APPENDIX

APPENDIX

TABLE OF CONTENTS

APPENDIX A

STATE OF MINNESOTA

IN SUPREME COURT

A17-1177

Office of Appellate Courts

[Filed: July 18, 2018]

William Fielding, Trustee of the Reid and Ann MacDonald Irrevocable GST Trust for Maria V. MacDonald, et al.,	)
Respondents,	)
v.	)
Commissioner of Revenue,	)
Relator.	)

Tax Court — Hudson, J.
Dissenting, Lillehaug, McKeig, JJ.
Took no part, Thissen, J.

Walter A. Pickhardt, Caitlin E. Abram, Faegre Baker Daniels LLP, Minneapolis, Minnesota, for respondents.

Lori Swanson, Attorney General, Michael P. Goodwin, Assistant Attorney General, Saint Paul, Minnesota, for relator.

SYLLABUS

1. When evaluating whether an income tax statute's residency classification violates the Due Process Clause as applied to a taxpayer, all relevant contacts between the taxpayer and the State during the tax year at issue are considered.

2. Because the taxpayers' relevant contacts with Minnesota during the tax year at issue are insufficient to permit Minnesota to tax those taxpayers as "resident trusts," Minn. Stat. § 290.01, subd. 7b(a)(2) (2016), is unconstitutional as applied to the taxpayers.

Affirmed.

OPINION

HUDSON, Justice.

Four irrevocable *inter vivos* trusts allege that their classification as "resident trusts" under Minn. Stat. § 290.01, subd. 7b (2016), is unconstitutional as applied to them under the Due Process Clauses of the United States and Minnesota Constitutions. The Trusts filed their 2014 Minnesota income tax returns under protest, then filed amended returns requesting refunds for the difference between taxation as resident trusts and taxation as non-resident trusts. After the Trusts' income tax refund requests were denied by the Commissioner of Revenue, the Trusts appealed to the Minnesota Tax Court. The Tax Court ruled in favor of the Trusts, holding that the statutory definition of "resident trusts," *see* Minn. Stat. § 290.01, subd. 7b(a)(2), violates the Due Process Clauses of the Minnesota and United States Constitutions as applied to the Trusts for the tax year at issue. Because we conclude that the Trusts lack sufficient relevant contacts with Minnesota during the applicable tax year to be permissibly taxed, consistent with due process, on all sources of income as residents, we affirm the decision of the Tax Court.

FACTS

This appeal of a Tax Court decision relates to four trusts (collectively, the "Trusts"): the Reid and Ann MacDonald Irrevocable GST Trust for Maria V. MacDonald (the "Maria Trust"); the Reid and Ann MacDonald Irrevocable GST Trust for Catherine Gray MacDonald (the "Catherine Trust"); the Reid and Ann MacDonald Irrevocable GST Trust for Laura Reid MacDonald (the "Laura Trust"); and the Reid and Ann MacDonald Irrevocable GST Trust for Vandever R. MacDonald (the "Vandever Trust"). Based on the parties' stipulation, the relevant facts for purposes of this appeal are undisputed.

Each of the Trusts was created on June 25, 2009, by grantor Reid MacDonald, then a domiciliary of Minnesota, and each trust was initially funded with shares of nonvoting common stock in Faribault Foods, Inc. ("FFI"), a Minnesota S corporation. The original trustee for all four trusts was a California domiciliary, Edmund MacDonald. Initially, grantor Reid MacDonald retained control over the trust assets. Thus, for Minnesota income tax purposes, the Trusts were "grantor type trusts" for the first 30 months of their existence. During this period, although the grantor (Reid MacDonald) was required to file Minnesota income tax returns, the Trusts were not required to do so. *See* Minn. Stat. § 290.01, subd. 7b(a) (2016) (explaining that the "income or gains of . . . [a grantor type] trust are taxable to the grantor or others treated as substantial owners" under the Internal Revenue Code).

On December 31, 2011, grantor Reid MacDonald relinquished his power to substitute assets in the Trusts. The Trusts therefore ceased to be "grantor type trusts" and became irrevocable on December 31, 2011. *See* Minn. Stat § 290.01, subd. 7b(a) ("[A] trust is considered irrevocable to the extent the grantor is not treated as the owner [of a trust]."). At the time the trusts became irrevocable, Reid MacDonald was domiciled in Minnesota. Based on Reid MacDonald's domicile in Minnesota when the Trusts became irrevocable, the Trusts were then classified as "resident trusts" under Minn. Stat. § 290.01, subd. 7b(a)(2).[1] Katherine Boone, a domiciliary of Colorado, became the sole Trustee for each of the Trusts on January 1, 2012.

After they ceased to be grantor-type trusts, the Trusts filed Minnesota income tax returns as resident trusts, without protest, in 2012 and 2013. On July 24, 2014, William Fielding, a domiciliary of Texas, became Trustee for the Trusts. Shortly thereafter, all shareholders of FFI stock, including the Trusts, sold their shares. Because the Trusts were defined to be Minnesota residents (as a result of grantor MacDonald's Minnesota domicile in 2011), they were subject to tax on the full amount of the gain from the 2014 sale of the FFI stock, as well on the full amount of

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[1] "Resident trust means a trust, except a grantor type trust, which . . . is an irrevocable trust, the grantor of which was domiciled in this state at the time the trust became irrevocable." Minn. Stat. § 290.01, subd. 7b(a)(2).

income from other investments.[2] *See* Minn. Stat. § 290.17, subd. 2(c) (2016) (providing that Minnesota taxes "resident trusts" on all "income or gains from intangible personal property," including investment income, "not employed in the business of the recipient of the income"). Had the Trusts not been deemed residents of Minnesota, those items of income would have been assigned to the Trusts' domicile and would not have been subject to Minnesota income taxation. *See* Minn. Stat. § 290.17, subd. 2(e) (2016).

The Trusts filed their 2014 Minnesota income tax returns under protest, asserting that the statute classifying them as resident trusts, Minn. Stat. § 290.01, subd. 7b(a)(2), was unconstitutional as applied to them. The Trusts then filed amended tax returns claiming refunds for the difference between the taxes owed as resident trusts and the taxes owed as nonresident trusts—a tax savings of more than $250,000 for each Trust.

The Commissioner of Revenue denied the Trusts' refund claims. The Trusts then appealed the Commissioner's orders denying the refund claims to the Minnesota Tax Court, asserting as-applied constitutional challenges under the state and federal Due Process Clauses[3] and the federal Commerce

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[2] In October 2014, Fielding approved the transfer of funds from the sale of the FFI stock to an investment account that was managed and administered by Wells Fargo in California. From October through December 2014, the Trusts earned income on these investment funds.

[3] Both the Minnesota and United States Constitutions state that no person shall be deprived of life, liberty, or property without due process of law. *See* U.S. Const. amend. XIV, § 1; Minn. Const.

Clause to section 290.01, subdivision 7b(a)(2). *Fielding v. Comm'r of Revenue*, Nos. 8911-R, 8912-R, 8913-R, 8914-R, 2017 WL 2484593, at *1–2 (Minn. T.C. May 31, 2017).

Deciding the appeals on cross-motions for summary judgment, the Tax Court framed the issue presented to it as: "Whether, for due process purposes, the domicile of the grantor alone is a sufficient connection with Minnesota to justify taxing the Trusts *as residents* (that is, on a tax base that includes intangible personal property *not* related to Minnesota)." *Id.* at *11. The Tax Court then considered "the proper scope" of the due process inquiry. *Id*. at *12. The Trusts argued that the Tax Court should limit the due process inquiry to the single factor identified in the statute that defines a resident trust— "the grantor's domicile at the time the Trusts became irrevocable." *Id.* The Commissioner, in contrast, argued that the court should consider "all the contacts between Minnesota and the Trusts" in the due process analysis. *Id*. Agreeing with the Commissioner, the Tax Court determined that all relevant contacts between the taxpayer and Minnesota should be considered, but concluded that the only relevant contact was the single factor identified in the statute; namely, the grantor's residency at the time the Trusts became irrevocable. *Id*. at *13.

The Tax Court ultimately concluded that "section 290.01, subdivision 7b(a)(2), as applied to the Trusts

art. I, § 7. We treat the due process protections in the United States Constitution and the Minnesota Constitution identically. *Schatz v. Interfaith Care Ctr.*, 811 N.W.2d 643, 657 (Minn. 2012). We therefore refer generally to the "Due Process Clause" rather than differentiating between the two Due Process Clauses.

for tax year 2014, violates the due process provisions of the Minnesota and United States constitutions." *Id.* at *20. Specifically, the court concluded that "Minnesota did not have a sufficient basis to tax the Trusts as 'residents'" because the grantor's domicile at the time the trust becomes irrevocable was not "a connection of sufficient substance" to support the exercise of taxing jurisdiction. *Id*. at *14, 19–20. According to the Tax Court, "Minnesota did not have subject matter jurisdiction over gain and income from . . . items of intangible personal property not located within Minnesota." *Id*. at *20. Having decided the case on due process grounds, the Tax Court did not reach the Trusts' claims under the Commerce Clause. *Id*. at *20 n.87.

Based on its conclusion that the statutory definition for a "resident trust," as applied to the Trusts, violated the Due Process Clause, the Tax Court held that "the Commissioner erred in denying the Trusts' refund claims," granted the Trusts' motions for summary judgment, and denied the Commissioner's motions for summary judgment. *Id.* at *20. The Commissioner appeals from the Tax Court's decision.

ANALYSIS

The questions presented by this appeal, which involve consideration of statutory language and constitutional challenges, are purely legal and subject to de novo review. *See Luther v. Comm'r of Revenue*, 588 N.W.2d 502, 506 (Minn. 1999). We presume that statutes are constitutional and hold the party asserting otherwise to a high burden to overcome that presumption. *Kimberly-Clark Corp. v. Comm'r of Revenue*, 880 N.W.2d 844, 848 (Minn. 2016).

I.

The dispute between the Trusts and the Commissioner implicates the extent of the Trusts' tax liability to Minnesota. If the Trusts are residents, Minnesota can tax the Trusts' worldwide income. *See Shaffer v. Carter*, 252 U.S. 37, 57 (1920) ("As to residents [the State] may, and does, exert its taxing power over [the taxpayers'] income from all sources . . . ."). If the Trusts are not residents, Minnesota's tax authority is restricted. *See* Minn. Stat. § 290.17, subd. 2(c) (describing the scope of the State's tax authority over a "resident trust"); *see also New York ex rel. Cohn v. Graves*, 300 U.S. 308, 312–13 (1937) (explaining that residence within a state establishes the state's authority to tax the receipt of income by the resident).

Before evaluating whether the Trusts' contacts with Minnesota were sufficient for taxation as residents consistent with due process, we must first determine the scope of our inquiry. The language of Minn. Stat. § 290.01, subd. 7b(a)(2), defines a "[r]esident trust," in relevant part, as "a trust, except a grantor type trust, which . . . is an irrevocable trust, the grantor of which was domiciled in this state at the time the trust became irrevocable." No other factors for determining residency are listed in the statute. Neither party argues that the statutory language is ambiguous; in fact, the parties stipulated that the statute's definition applies to the Trusts and that the Trusts filed their 2014 Minnesota tax returns (under protest) as residents.

Citing *Rew v. Bergstrom*, 845 N.W.2d 764, 780 (Minn. 2014), the Commissioner asserts that in an as-applied challenge based on the Due Process Clause, we must examine all facts and circumstances underlying the Commissioner's action, including the "practical operation of the tax residency statute" in this case and the multiple contacts between Minnesota and the Trusts. The Trusts argue that although their due process claim is an as-applied challenge, when evaluating the constitutionality of the statute, our consideration is limited to the single factor identified in the statute for determining residency—namely, the domicile of the grantor at the time the Trusts became irrevocable. The Trusts contend that to consider other facts, as the Commissioner urges, would effectively require that we add language to the statute.

We have said that a tax will satisfy due process if (1) there is a "minimum connection" between the state and the person, property, or transaction subject to the tax, and (2) the income subject to the tax is rationally related to the benefits conferred on the taxpayer by the State. *See Luther*, 588 N.W.2d at 508–09. In applying these requirements in the context of a due process challenge to a taxpayer's status as a resident for income tax purposes, we consider factors beyond those in the challenged residency statute. In *Luther*, for example, we considered "the many services, benefits, and protections afforded [the taxpayer] by Minnesota in her right to receive and enjoy her income." *Id.* at 509. Ultimately, after concluding that the taxpayer had "enjoyed the many services, benefits, and protections Minnesota provided for her" for the majority of the tax year, we held that the taxpayer's total contacts with Minnesota were sufficient to meet due process requirements for taxing her as a resident. *Id.*

Luther and other decisions involving due process challenges to taxing statutes demonstrate that we look beyond the statutory definition that identifies who is subject to a tax in order to evaluate the relationship between the income taxed and the benefits provided by the state.[4] This analysis is not, as the Trusts claim, a matter of adding language to the statute. We are not redefining a resident trust; we are simply evaluating, as we have in other cases, all the relevant facts when considering whether the application of the statutory definition would be consistent with due process in this case.[5] Therefore, in accordance with our past decisions,

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[4] *See, e.g.*, *Watlow Winona, Inc. v. Comm'r of Revenue*, 495 N.W.2d 427, 434 (Minn. 1993) (explaining that "once a state has decided to tax a corporation as a unitary business using an apportionment formula," the taxation is unconstitutional if "the income attributed to the State is in fact 'out of all appropriate proportions' to the business transacted in that State" (citations omitted)); *Soo Line R.R. Co. v. Comm'r of Revenue*, 377 N.W.2d 453, 456 (Minn. 1985) (stating that we consider whether a "tax is fairly apportioned to activities within the state" in a due process challenge to a method of apportionment); *Harris v. Comm'r of Revenue*, 257 N.W.2d 568, 571 (Minn. 1977) (finding "no nexus between [Minnesota] and the taxpayer's income-producing activity in the State of Georgia" for purposes of a due process challenge to a statute that disallowed deductions on Minnesota returns for the expenses of moving outside of Minnesota for work).

[5] The Tax Court engaged in statutory construction in reaching its conclusion that the only relevant factor was the single factor contained in the resident trust definition. *See Fielding*, 2017 WL 2484593, at *12–13. However, both parties agree that the statute is unambiguous in its plain language, so there is no need to construe the statute. Moreover, we do not read the statute's language as an attempt by the Legislature to constrain the scope of judicial authority when considering substantive due process challenges. *See generally Luther*, 588 N.W.2d at 508–09.

we conclude that in the context of a due process challenge to the State's taxation of a taxpayer as a resident, we will examine all relevant contacts between the taxpayer and the State, including the relationship between the income attributed to the state and the benefits the taxpayer received from its connections with the state. *See Luther*, 588 N.W.2d at 508–09.

II.

We next consider whether the Trusts' contacts with Minnesota are sufficient, under the Due Process Clause, to permit them to be taxed as Minnesota residents. A state's tax satisfies due process if there is (1) some "minimum connection" between the state and the entity subject to the tax, and (2) a "rational relationship" between the income the state seeks to tax and the protections and benefits conferred by the state. *Id.* at 508; *see also Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 778 (1992) (explaining that in a due process challenge, "there must be a connection to the activity itself, rather than a connection only to the actor the State seeks to tax," and the "basic principle" is that the "State's power to tax . . . activities is justified by the protection, opportunities and benefits the State confers on those activities" (citation omitted) (internal quotation marks omitted)).

Here, we are asked to decide not whether any particular *source* of trust income can be constitutionally taxed by Minnesota. Indeed, the Trusts do not dispute the constitutionality of taxing their Minnesota-sourced income and have acknowledged that the apportioned flow-through operating income from FFI is subject to tax by Minnesota. The Trusts' Minnesota tax returns report this income.

Instead, the question we must decide instead is whether Minnesota may permissibly tax *all* sources of income to the Trusts simply because it has classified the Trusts as residents based on events that pre-date the tax year at issue (2014). The dispute here is whether the undisputed facts in addition to the domicile of the grantor in 2011 (when the Trusts were made irrevocable) provide a sufficient basis under the Due Process clause to support Minnesota's taxation of *all* of the income of the Trusts.

The Commissioner contends that she can constitutionally tax the Trusts' worldwide income based on several contacts between Minnesota and the Trusts, asserting that the Trusts "ow[e] their very existence" to Minnesota. Specifically, the grantor, Reid MacDonald, was a Minnesota resident when the Trusts were created, was domiciled in Minnesota when the Trusts became irrevocable, and was still domiciled in Minnesota in 2014. The Trusts were created in Minnesota, with the assistance of a Minnesota law firm, which drafted, and until 2014 retained, the trust documents. The Trusts held stock in FFI, a Minnesota S corporation. The Trust documents provide that questions of law arising under the Trust documents are determined in accordance with Minnesota law. Finally, one beneficiary, Vandever MacDonald, has been a Minnesota resident at least through the tax year at issue.

The Trusts, on the other hand, note that no Trustee has been a Minnesota resident, the Trusts have not been administered in Minnesota, the records of the Trusts' assets and income have been maintained outside of Minnesota, some of the Trusts' income is derived from investments with no direct connection to Minnesota, and three of the four trust beneficiaries reside outside of Minnesota.

We conclude that the contacts on which the Commissioner relies are either irrelevant or too attenuated to establish that Minnesota's tax on the Trusts' income from all sources complies with due process requirements. We reach this conclusion for the following three reasons.

First, the *grantor's* connections to Minnesota—the Minnesota residency of Reid MacDonald in 2009, when the Trusts were established; in 2011, when the Trusts were made irrevocable; and in 2014, when the Trusts sold the FFI stock—are not relevant to the relationship between the *Trusts'* income that Minnesota seeks to tax and the protection and benefits Minnesota provided to the *Trusts'* activities that generated that income. The relevant connections are Minnesota's connection to the trustee, not the connection to the grantor who established the trust years earlier.

A trust is its own legal entity, with a legal existence that is separate from the grantor or the beneficiary. *See Greenough v. Tax Assessors of Newport*, 331 U.S. 486, 495–96 (1947) ("The citizenship of the trustee and not the seat of the trust or the residence of the beneficiary is the controlling factor."); *Anderson v. Wilson*, 289 U.S. 20, 27 (1933) (noting that "the law has seen fit" to consider a trust "for income tax purposes as a separate existence"). Here, grantor Reid MacDonald is not the taxpayer, the Trusts are. Moreover, regardless of the grantor's personal connections with Minnesota, after 2011 he no longer had control over the Trusts' assets. *See, e.g., Safe Deposit & Tr. Co. of Baltimore v.*

Virginia, 280 U.S. 83, 91–93 (1929) (concluding that Virginia, where the grantor resided but had no "control or possession" over the intangible assets of the trust, which was domiciled in Maryland, could not impose a tax on those assets); *Taylor v. State Tax Comm'n*, 445 N.Y.S.2d 648, 649 (N.Y. App. Div. 1981) (holding that New York could not impose an income tax on trust property because "possession and control" of those assets was held by trustees who were not residents of or domiciled in New York). For similar reasons, the Minnesota residency of beneficiary Vandever MacDonald does not establish the necessary minimum connection to justify taxing the Trusts' income.[6] *See Greenough*, 331 U.S. at 495–96.

[6] As a domiciliary of Minnesota, Vandever MacDonald filed a Minnesota resident income tax return for 2014. The permissibility of taxing Vandever MacDonald as an individual for disbursements from the Vandever Trust is entirely separate from taxing the Vandever Trust *as a resident*. Even if the domicile of a beneficiary were an appropriate factor to consider, it would not support taxing the three Trusts that have non-resident beneficiaries. Vandever MacDonald's status as a contingent beneficiary for the Maria Trust, Catherine Trust, and Laura Trust is also irrelevant, both because of the distinction between the entities subject to tax (Vandever individually as distinguished from the Trusts) and because the contingency did not come to pass during the tax year at issue.

The dissent reaches a different conclusion by relying on T. *Ryan Legg Irrevocable Trust v. Testa*, 75 N.E.3d 184 (Ohio 2016). But that case is distinguishable because the Ohio statute that defines trust residency considers whether the grantor is a resident at the time the trust is established "and whether a 'qualifying beneficiary' is an Ohio resident." *Id*. at 195–96. In addition, the relevant contacts at issue in that case regarding trust creation, funding, and tax liability spanned a mere 3 months. *Id*. at 186–87. Here, in contrast, the Commissioner and the dissent look back, several years in some cases, to find contacts by persons other than the Trust and the trustees.

Nor do we find the grantor's decision to use a Minnesota law firm to draft the trust documents to be relevant. The parties stipulated that the law firm represented the grantor. Other than retaining the original signed trust documents, nothing in the record establishes that the law firm represented the Trusts or the Trustees in connection with the activities that led to the income that the State seeks to tax, let alone during the tax year at issue.[7] We are unwilling to attribute legal significance to the storage of the original signed trust documents in Minnesota, when this act may have been nothing more than a service or convenience extended to the firm's client—the grantor.

Second, the Trusts did not own any physical property in Minnesota that might serve as a basis for taxation as residents. *See, e.g.*, *Westfall v. Dir. of Revenue*, 812 S.W.2d 513, 514 (Mo. 1991) (upholding Missouri's tax on a trust, in part because the trust owned real property in the state). The Commissioner urges us to hold that the Trusts may be taxed as residents due to their connections to FFI, a Minnesota S corporation, and it is undisputed that the Trusts held interests in *intangible property*, FFI stock. Although FFI was incorporated in Minnesota and held physical property within the state, the intangible property that generated the Trusts' income was *stock* in FFI and funds held in investment accounts. These intangible assets were held outside of Minnesota, and thus do not

[7] The same law firm that represented the grantor now represents the Trusts in this tax proceeding. But the record does not establish when the Trusts retained the law firm for purposes of this challenge, and in any event, this representation is not relevant to the activities that generated the income that the State seeks to tax.

serve as a relevant or legally significant connection with the State. *See, e.g.*, *Safe Deposit & Tr. Co.*, 280 U.S. at 92 (stating that intangible assets held by a trustee located in Maryland "did not and could not follow" the grantor and beneficiaries who were domiciled in Virginia); *In re Swift*, 727 S.W.2d 880, 881–82 (Mo. 1987) (concluding that the "creation and funding" of the trusts in Missouri with intangible assets that the trustee "held, managed and administered in Illinois" did not allow Missouri to tax the trust's income); *Mercantile-Safe Deposit & Tr. Co. v. Murphy*, 242 N.Y.S.2d 26, 28 (N.Y. App. Div. 1963) (concluding that New York, which was the grantor's domicile, could not tax the trust's income from intangible assets held in Maryland).[8]

Third, we do not find the contacts with Minnesota that pre-date 2014, the tax year at issue, by the grantor, the Trusts, or the beneficiaries, to be relevant. We have evaluated a taxpayer's contacts with Minnesota, for due process purposes, in the tax year at issue. *See Luther*, 588 N.W.2d at 509 (explaining that the taxpayer had the "opportunity to enjoy the many services, benefits, and protections" provided by the State for at least "the majority of" the tax year at

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[8] We relied on the doctrine of *mobilia sequuntur personam* ("movables follow the [law of the] person") in *Luther* for the proposition that intangible assets such as trust income have no particular situs for tax purposes. *See* 588 N.W.2d at 511–12. Here, the taxpayer—holder of the legal title to the stock in FFI and the other income-producing intangible assets—is the Trustee, who, it is undisputed, is not a Minnesota resident. Intangible assets are appropriately taxed as being resident in the jurisdiction where the owner of legal title—the Trustee—is a resident. *See Greenough*, 331 U.S. at 495–96; *Safe Deposit & Tr. Co.*, 280 U.S. at 93.

issue). Other courts have also held that the relevant facts for evaluating the sufficiency of a taxpayer's contacts are drawn from the tax year at issue. *See, e.g.*, *Linn v. Dep't of Revenue*, 2 N.E.3d 1203, 1210 (Ill. App. Ct. 2013) ("[W]hat happened historically with the trust in Illinois courts and under Illinois law has no bearing on the 2006 tax year."); *Potter v. Taxation Div*., 5 N.J. Tax 399, 404–05 (N.J. Tax Ct. 1983) (declining to rely on the trust's receipt of the grantor's assets, which "occurred prior to the tax year in question," to allow the state to tax).

There is good reason to focus on the taxpayer's contacts in the tax year at issue. The direct link between the activities that generated the income in the year at issue and the protections provided by the State in that same year establishes the necessary rational relationship that justifies the tax. In contrast, allowing the State to look to historical contacts unrelated to the tax year at issue risks leaving taxpayers unaware of whether or when their contacts with Minnesota may justify the imposition of a tax. *See Luther*, 588 N.W.2d at 508 ("Due process deals with the fairness of the tax at issue and ensures that the taxpayer has adequate notice that she may be subject to the tax.").

In addition, allowing the State to pick and choose among historical facts unrelated to the tax year at issue is unworkable. This ad hoc approach could force taxpayers to challenge tax liability annually until a court determines that the past contacts have sufficiently decayed such that they are no longer sufficient to support taxation as a resident. Nor can we see any reasonable means of determining when the decay will be sufficient. *Accord Blue v. Dep't of*

Treasury, 462 N.W.2d 762, 764–65 (Mich. Ct. App. 1990) ("We analogize the present case to a hypothetical statute authorizing that any person born in Michigan to resident parents is deemed a resident and taxable as such, no matter where they reside or earn their income. We believe this would be clearly outside of the state's power to impose taxes.").

Thus, we are left to consider the extremely tenuous contacts between the Trusts (or their Trustees) and Minnesota during tax year 2014. The Trustees had almost no contact with Minnesota during the applicable tax year. All trust administration activities by the Trustees occurred in states other than Minnesota. Boone never traveled to Minnesota during her time as a Trustee. Fielding traveled to Minnesota for a weekend in the fall of 2014 to attend a wedding, but he never traveled to Minnesota for any purposes related to the Trusts. This level of contact is clearly not enough to establish residency for taxation purposes.

We acknowledge that "questions of law" that may arise under the trust agreements are determined by the laws of Minnesota. Standing alone, however, this choice-of-law provision is not enough to permissibly tax the Trusts as residents. Our laws protect residents and non-residents alike. We will not demand that every party who chooses to look to Minnesota law—not necessarily to invoke the jurisdiction of Minnesota's courts—must pay resident income tax for the privilege. Of note here, unlike cases in other states that considered testamentary trusts, the *inter vivos* trusts at issue here have not been probated in Minnesota's courts and have no existing relationship to the courts distinct from that of the trustee and trust assets. *See*

District of Columbia v. Chase Manhattan Bank, 689 A.2d 539, 544 (D.C. 1997); *In re Swift*, 727 S.W.2d at 882.

The dissent places significance on the Trusts' funding from shares of common stock in a Minnesota S corporation, relying on *Luther*'s language regarding the protections provided by state law to corporations affiliated with the nondomiciliary resident taxpayer. *See* 588 N.W.2d at 509. In *Luther*, this benefit was one of "*many* services, benefits, and protections" provided to the taxpayer *during the year* in which the tax was imposed. *Id.* (also noting that "*for the majority of 1990*, Luther" enjoyed these state-provided benefits (emphasis added)).[9] Due process does not merely require that *some* benefit be conferred on the taxpayer. Due process requires that there be a rational relationship between the amount the State asks a taxpayer to contribute and the amount of "services, benefits, and protections" the taxpayer receives and enjoys. *Id.*

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[9] Thus, *District of Columbia v. Chase Manhattan Bank*, 689 A.2d 539 (D.C. 1997), on which the dissent relies, is distinguishable. There, the court relied on the probate proceedings "in the courts of the District of Columbia" to show "a relationship to the District distinct from the relationship, if any, between the District and the trustee or trust assets." *Id*. at 544. Unlike the taxpayer in *Luther*, who intentionally sought the benefits, protections, and services that Minnesota provided in the year in which she was subject to Minnesota tax, and unlike the taxpayer in *Chase Manhattan Bank*, in which a testamentary trust consented to the "continuing supervisory jurisdiction" of the District of Columbia courts, including for "litigation" and "claims," *id*. at 540–41, nothing in the record here shows that the Trustee or any of the Trusts have actively or actually sought the benefits or protections provided by Minnesota in the year in which Minnesota seeks to tax the Trusts.

The dissent insists that there *is* a rational relationship between the benefits conferred on the Trusts and taxing the Trusts in 2014 on their full worldwide income as residents. In reaching this conclusion, the dissent ignores the numerous stipulated facts demonstrating that the Trusts had almost no contact with the State during the tax year at issue. The Trustees, not the grantor, made all decisions regarding the Trusts, including whether to sell the stock in FFI. These decisions were made entirely outside of Minnesota, and all 2014 Trust records of assets and income were maintained outside of Minnesota. The Trustees never travelled to Minnesota for Trust business in 2014 and were never plaintiffs or defendants in any other suit before Minnesota courts in their capacity as Trustees. When the full context is viewed, it becomes clear that the Trusts did not enjoy a level of services, benefits, and protections anywhere near those enjoyed by the taxpayer in *Luther*, 588 N.W.2d at 509.[10]

Accordingly, even when the additional contacts the Commissioner cites are considered in combination, the State lacks sufficient contacts with the Trusts to support taxation of the Trusts' entire income as residents consistent with due process. The State cannot fairly ask the Trusts to pay taxes as residents in return for the existence of Minnesota law and the physical

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[10] The dissent also refers to benefits the State is alleged to have provided to the beneficiaries of the Trusts. This argument improperly conflates the tax status of the beneficiaries with the tax status of the Trusts. As discussed above, whether and how Minnesota can tax resident beneficiaries is entirely distinct from whether the State can tax the Trusts, which are separate legal entities.

storage of trust documents in Minnesota. Attributing all income, regardless of source, to Minnesota for tax purposes would not bear a rational relationship with the limited benefits received by the Trusts from Minnesota during the tax year at issue. We therefore hold that Minn. Stat. § 290.01, subd. 7b(a)(2), is unconstitutional as applied to the Trusts.[11]

CONCLUSION

For the foregoing reasons, we affirm the decision of the Tax Court.

Affirmed.

THISSEN, J., not having been a member of this court at the time of submission, took no part in the consideration or decision of this case.

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[11] Because we hold that the application of Minn. Stat. § 290.01, subd. 7b, to the Trusts is unconstitutional under the Due Process Clause, we express no opinion on the Commerce Clause arguments raised by the parties.

DISSENT

LILLEHAUG, J. (dissenting).

I respectfully dissent. During the tax year at issue, the four irrevocable *inter vivos* trusts (the Trusts) had sufficient relevant contacts with Minnesota such that the Trusts' classification as Minnesota "resident trusts" under Minn. Stat. § 290.01, subd. 7b(a)(2) (2016)—and subsequent taxation—did not violate the Due Process Clause. Nor did Minnesota's taxation of the Trusts implicate the Commerce Clause.

I.

At the threshold, I agree with the majority's analytical framework. I agree that the taxpayer "bears a heavy burden" to demonstrate that Minnesota's taxation of the Trusts is unconstitutional. *See Kimberly-Clark Corp. v. Comm'r of Revenue*, 880 N.W.2d 844, 848 (Minn. 2016). And I agree that the Tax Court erred in concluding that the only relevant contact between the Trusts and Minnesota was the single factor of the grantor's residency at the time the Trusts became irrevocable. The correct method of analysis, as the court holds in Part I of the opinion, is to consider all of the "services, benefits, and protections afforded [the taxpayer] by Minnesota." *Luther v. Comm'r of Revenue*, 588 N.W.2d 502, 509 (Minn. 1999).

My disagreement is with Part II of the court's opinion, which concludes that, under the Due Process Clause, the Trusts' contacts with Minnesota were insufficient to permit them to be taxed as Minnesota residents. Considering all relevant factors, I conclude that it was constitutional for Minnesota to tax the Trusts.

The Due Process Clause provides that the government shall not "deprive any person of life, liberty, or property, without due process of law." U.S. Const. amend. XIV, § 1; *see also* Minn. Const. art. I, § 7. In the taxation context, due process serves to "ensure[] that the taxpayer has adequate notice that she may be subject to the tax." *Luther*, 588 N.W.2d at 508. This court has held that, for a tax to survive a due-process challenge, "there must be (1) 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax' and (2) a rational relationship between 'the income attributed to the State for tax purposes [and the] values connected with the taxing State.'" *Id.* (quoting *Quill Corp. v. North Dakota*, 504 U.S. 298, 307 (1992)).[1] The "minimum connection" requirement "has been likened to the minimum contacts necessary to establish personal jurisdiction." *Id.*

With this standard in mind, due process has been satisfied here. First, there is a "minimum connection" between Minnesota and the Trusts. From their creation, the Trusts were Minnesota residents. They were created by Reid MacDonald, a Minnesota resident. The Trusts were created to hold almost exclusively Minnesota assets—the common stock of a Minnesota S corporation—over which Minnesotan MacDonald retained control. Further, the trust instruments themselves instruct the trustee—wherever

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[1] The United States Supreme Court has since overturned *Quill* to the extent that *Quill*'s interpretation of the "substantial nexus" prong of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), "is an incorrect interpretation of the Commerce Clause." *South Dakota v. Wayfair, Inc.*, ___ U.S. ___, ___, 138 S. Ct. 2080, 2092 (2018).

located—to apply the Minnesota Revised Uniform Principal and Income Act and to resolve all questions of law arising under the trust agreements according to "the laws of the State of Minnesota."

Most importantly, when MacDonald made the Trusts irrevocable in 2011, he did so as a Minnesota domiciliary. He was on statutory notice that, as a Minnesotan, his decision would cause the Trusts to become Minnesota "resident trusts." *See* Minn. Stat. § 290.01, subd. 7b(a)(2) (2016). When a Minnesota grantor knowingly chooses to create a Minnesota resident trust and the trust itself incorporates Minnesota law, why would it be unconstitutional for Minnesota to tax that trust? Put another way: how can it violate due process for a state to tax its residents (in this case, the Trusts) as residents? Other courts have provided a clear answer to this question—it cannot.[2] *See T. Ryan Legg Irrevocable Tr. v. Testa*, 75 N.E.3d 184, 197–98 (Ohio 2016) (holding that where "an Ohio resident . . . conducted business in significant part in Ohio through the corporate form and who disposed of his business and corporate interest . . . by means of a trust that he created to accomplish his objectives for himself and his family," that resident's Ohio contacts were "material for constitutional purposes"); *see also*

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[2] This position is also supported by leading scholars in the field of tax law. *See* 2 J. Hellerstein & W. Hellerstein, *State Taxation* ¶ 20.09[2][b], p. 20-211 (3d ed. 2017) (hereinafter Hellerstein & Hellerstein) ("[W]e believe it unlikely that the Supreme Court would hold today . . . that the Due Process Clause bars the state in which a resident settlor or decedent created a trust from taxing income accumulated by the trust from intangibles held by the trustee who resides outside the state and administers the trust there.").

District of Columbia v. Chase Manhattan Bank, 689 A.2d 539, 543 (D.C. 1997) (holding that the District of Columbia could "tax a testamentary trust throughout its entire existence even if its only connection to the District is that the testator was domiciled there at the time of death"). Indeed, here the Trusts "owe[] [their] very existence to the laws" of Minnesota. *Chase Manhattan Bank*, 689 A.2d at 543.[3]

Second, there is a rational relationship between the Trusts' income and the protection and benefits that Minnesota confers upon them. The Trusts were funded with shares of common stock in a Minnesota S corporation. *See Luther*, 588 N.W.2d at 509 (noting that the relator received benefits from the state because "[o]n every day of the year, state laws protected . . . the corporations with which she was affiliated"). The choice-of-law provision in the trusts invoke the benefits and protections of Minnesota laws. *See Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 482 (1985) ("Nothing in our cases . . . suggests that a choice-of-law *provision* should be ignored in considering whether a defendant has 'purposefully invoked the benefits and protections of a State's laws' for jurisdictional purposes."). Similarly, the requirement that the trustee "apply the rules stated in the Minnesota Revised Uniform Principal and Income Act" ensures that the Trusts' beneficiaries receive the benefits and protections of Minnesota law. Further, one of the trust beneficiaries

[3] The majority notes that *Chase Manhattan Bank* dealt with a testamentary trust, whereas here we are dealing with *inter vivos* trusts. Although *Chase Manhattan Bank* left open the question of whether its holding would apply to *inter vivos* trusts, 689 A.2d at 547 n.11, I see no sound reason for treating the two types of trusts differently in this context.

is still domiciled in the state. Minnesota can properly require the Trusts to contribute to the State for costs associated with providing these benefits, services, and protections to the Trusts, the trustee, and the beneficiaries.

Therefore, I would conclude that the "minimum connection" and "rational relationship" requirements of due process have been satisfied here.

Much of my analysis considers events that happened prior to 2014—the tax year at issue here. The majority asserts that what happened before 2014 is not "particularly relevant." To the contrary: what happened before 2014 created the legal structure of the very Trusts at issue.

The majority also observes that by 2014 circumstances had changed, making any remaining connections between the Trusts and Minnesota "extremely tenuous contacts." It is true that, in 2014, a non-Minnesota trustee was in place and the Minnesota S corporation stock was sold. But the sale occurred in the second half of 2014. Thus, it is not as if the trust assets in 2014 had no connection to Minnesota; indeed, most of the Trusts' income was solidly connected to the state. In sum, contrary to the majority's conclusion, the remaining connections to Minnesota in 2014 were both relevant and substantial.

The majority cites several United States Supreme Court decisions to support its conclusion that the citizenship of the *trustee*, not the grantor, is the controlling factor in a due-process analysis. The majority's reliance on these decisions is misplaced. The majority cites *Greenough v. Tax Assessors of Newport*, 331 U.S. 486 (1947), for the proposition that "[t]he citizenship of the trustee and not that of the trust or the residence of the beneficiary is the controlling factor." *Id.* at 495–96. But this language arose in the context of explaining the relevance of a trustee's citizenship when determining whether a federal court has diversity jurisdiction over a trust dispute. *See id.* This comment on an unrelated legal principle is dicta.

The majority also cites *Anderson v. Wilson*, 289 U.S. 20 (1933), for the proposition that the grantor's domicile is not relevant when performing a due process analysis. But the issue in *Wilson* was "whether the difference between the value of real estate at the death of a testator and the proceeds realized thereafter upon a sale by the trustees may be deducted as a loss by the taxpayer," the trust beneficiary. *Id.* at 21. In concluding that the beneficiary was not allowed to deduct the loss, the Court noted that "the trust, and not the taxpayer, has suffered the loss resulting from the sale of the [real estate]" and the law treats trusts "as a separate existence . . . claiming and receiving its own appropriate [tax] deductions." *Id.* at 26–27. *Wilson* is devoid of any due-process analysis and thus has little persuasive value here.[4]

[4] The majority also cites *Safe Deposit & Trust Co. of Baltimore v. Virginia*, 280 U.S. 83 (1929), which held that Virginia did not have the right to tax securities that were "property within Maryland" and to which "nobody within Virginia ha[d] the present right to their control or possession, or to receive income therefrom, or to cause them to be brought physically within her borders." *Id.* at 91. But, in 2014, the Trusts were more closely connected to Minnesota than the securities at issue in *Safe Deposit & Trust Co.* Further, a driving concern behind the decision in *Safe Deposit & Trust Co.* was that permitting Virginia to tax the securities would allow "a

In sum, the Trusts have not met the heavy burden to show a violation of the Due Process Clause.

II.

Because I conclude that Minnesota's taxation of the Trusts did not violate due process, I would reach, and reject, the Trusts' alternative argument, that the taxation violated the Commerce Clause.

The Commerce Clause states that "[t]he Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the several States." U.S. Const. art. I, § 8, cl. 3. In addition to the affirmative grant of power to Congress, courts have long held that the Commerce Clause also contains an "implied negative command"—the dormant Commerce Clause. *Luther*, 588 N.W.2d at 510. The dormant Commerce Clause commands that "states cannot, through the enactment of statutes or regulations, discriminate against or unduly burden interstate commerce." *Id.* "A tax may be consistent with due process but still violate the Commerce Clause." *Id.* The Trusts argue that Minn. Stat. § 290.01, subd. 7b(a)(2) violates the dormant Commerce Clause.

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double and oppressive assessment." *Id.* at 94. This same concern is not present here. Under Minn. Stat. § 290.01, subd. 7b(a), to be taxed as a resident trust, the grantor (or decedent) must be domiciled in Minnesota at the time the trust becomes irrevocable (or at the time the decedent dies). Moreover, courts and legal scholars have expressed doubt as to whether *Safe Deposit & Trust Co.* remains good law. *See Chase Manhattan Bank v. Gavin*, 733 A.2d 782, 803 (Conn. 1999); 2 Hellerstein & Hellerstein ¶ 20.09[2][b].

Before considering the merits of a Commerce Clause challenge, the gateway inquiry is "whether the challenged statute implicates the Commerce Clause." *Chapman v. Comm'r of Revenue*, 651 N.W.2d 825, 832 (Minn. 2002). The purpose of the dormant Commerce Clause is to "protect[] markets and participants in markets." *Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 300 (1997). Accordingly, to implicate the dormant Commerce Clause, the taxpayer must demonstrate that "application of [Minn. Stat. § 290.01, subd. 7b(a)(2)] has a substantial effect on an identifiable interstate economic activity or market." *Luther*, 588 N.W.2d at 511. In other words, "the dormant Commerce Clause will not apply unless there is actual or prospective competition between entities in an identifiable market *and* state action that either expressly discriminates against or places an undue burden on interstate commerce." *Stelzner v. Comm'r of Revenue*, 621 N.W.2d 736, 740–41 (Minn. 2001). Further, the Commerce Clause is not implicated unless the impact on interstate commerce is "more than merely incidental." *Id.* at 741.

Here, the Trusts have not demonstrated that application of the statute "has a substantial effect on an identifiable interstate economic activity or market." *Luther*, 588 N.W.2d at 511. Nor have the Trusts shown that any impact on interstate commerce would be "more than merely incidental." *Stelzner*, 621 N.W.2d at 741. Accordingly, the Trusts have not met their "heavy burden" to show that Minnesota's definition of "resident trust" implicates the Commerce Clause. *See Kimberly-Clark Corp.*, 880 N.W.2d at 848.

Because I would conclude that Minn. Stat. § 290.01, subd. 7b(a)(2), as applied here, is constitutional under the Due Process Clause and does not implicate the Commerce Clause, I respectfully dissent.

MCKEIG, Justice (dissenting).

I join in the dissent of Justice Lillehaug.

APPENDIX B

STATE OF MINNESOTA
COUNTY OF RAMSEY
TAX COURT
REGULAR DIVISION

File Nos. 8911-R, 8912-R, 8913-R, 8914-R

[Filed: May 31, 2017]

William Fielding, Trustee of the Reid and Ann MacDonald Irrevocable GST Trust for Maria V. MacDonald, et al.,

Appellants,

v.

Commissioner of Revenue,

Appellee.

ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

These matters came before The Honorable Bradford S. Delapena, Judge of the Minnesota Tax Court, on the parties' cross-motions for summary judgment.

Walter A. Pickhardt and Caitlin E. Abram, Faegre Baker Daniels LLP, represent appellants William Fielding, Trustee of the Reid and Ann MacDonald Irrevocable GST Trust for Maria V. MacDonald, et al.

Kyle W. Wislocky, Assistant Minnesota Attorney General, represents appellee Commissioner of Revenue.

Each appellant Trust appeals an order of the Minnesota Commissioner of Revenue denying an income tax refund claim.[1] As relevant here, Minnesota law defines "resident trust" in part as "an irrevocable trust, the grantor of which was domiciled in this state at the time it became irrevocable." Minn. Stat. § 290.01, subd. 7b(a)(2) (2016). Under this provision, once an *inter vivos* trust becomes irrevocable, it is forever treated as a "resident trust" based on the single circumstance that its grantor "was domiciled in this state at the time the trust became irrevocable." No other connection with Minnesota is then, or ever, required or even relevant.

Residency generally authorizes a state to tax a taxpayer's worldwide income regardless of source. Accordingly, if a trust qualifies as a Minnesota *resident* trust, "[i]ncome or gains from intangible personal property *not employed in the business of the recipient"* are "assigned to"—and thus taxed by—Minnesota. Minn. Stat. § 290.17, subd. 2(c) (2016) (emphasis added). In contrast, such income and gains earned by a nonresident trust are *not* assigned to Minnesota.

[1] Stip. ¶ 19. The four appellant trusts are the Reid and Ann MacDonald Irrevocable GST Trust for Maria V. MacDonald ("Maria Trust"); the Reid and Ann MacDonald Irrevocable GST Trust for Catherine Gray MacDonald ("Catherine Trust"); the Reid and Ann MacDonald Irrevocable GST Trust for Laura Reid MacDonald ("Laura Trust"); and the Reid and Ann MacDonald Irrevocable GST Trust for Vandever R. MacDonald ("Vandever Trust") (collectively, the "Trusts").

Minn. Stat. § 290.17, subd. 2(e) (2016). Thus, by defining a trust as a "resident trust," Minnesota asserts authority to tax trust income and gains from all sources—including income and gains from intangible assets having no relation to Minnesota.

Each Trust filed a 2014 Minnesota income tax return treating itself as a "resident trust" and paid tax (under protest) on income and gains from intangible personal property the Trust asserted had no relation to Minnesota.[2] Each Trust then filed an amended return treating itself as a nonresident trust, computing its tax liability by excluding income and gains from intangible personal property not related to Minnesota, and requesting a refund. Applying section 290.01, subdivision 7b(a)(2), which defines each Trust as a "resident trust," the Commissioner denied the Trusts' refund claims. The Trusts timely appealed to this court.

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[2] A trust is a fiduciary relationship, Restatement (Third) of Trusts § 2 (2003), that is taxed as an entity, *Anderson v. Wilson,* 289 U.S. 20, 27 (1933). It is well settled that the domicile of the trustee—the person with possession and legal title of trust of assets—may tax a trust. *See Greenough v. Tax Assessors of City of Newport,* 331 U.S. 486, 497 (1947) (commenting that nothing in the Court's jurisprudence "leads to the conclusion that a state may not tax intangibles in the hands of a resident trustee of an out-of-state trust"); *Safe Deposit* & *Trust Co. of Balt. v. Virginia,* 280 U.S. 83, 91 (1929) ("Manifestly, the securities are subject to taxation in Maryland where they are in the actual possession of the trust company - holder of the legal title."). Sufficient connections may permit other states to tax a trust as well. Because the Trusts' trustees were domiciled outside of Minnesota during 2014, the question here is whether—consistent with due process—Minnesota may tax the Trusts as "residents," on their worldwide income.

The Trusts do not dispute that they qualify as "resident trusts" under section 290.01, subdivision 7b(a)(2). Instead, they contend that—as applied to them—the statute violates the due process provisions of the Minnesota and United States constitutions and the Commerce Clause of the Federal Constitution. The parties have filed cross-motions for summary judgment on the Trusts' constitutional claims. We grant the Trusts' motions for summary judgment and deny the Commissioner's motions.

The court, upon all the files, records, and proceedings herein, now makes the following:

ORDER

1. The Trusts' motions for summary judgment are granted.
2. The Commissioner's motions for summary judgment are denied.

IT IS SO ORDERED. THIS IS A FINAL ORDER. LET JUDGMENT BE ENTERED ACCORDINGLY.

BY THE COURT,

/s/Bradford S. Delapena
Bradford S. Delapena, Judge
MINNESOTA TAX COURT

DATED: May 31, 2017

MEMORANDUM

I. FACTUAL AND PROCEDURAL BACKGROUND

The issue in these consolidated cases is whether Minnesota may lawfully tax capital gains that appellant Trusts realized during 2014 from the sale of certain stock, along with other income from intangible personal property located outside of Minnesota. In conjunction with their cross-motions for summary judgment, the parties filed an extensive stipulation of facts concerning the creation and funding of the Trusts; the trustees and beneficiaries; the Trusts' income and gains during 2014; and the history of the parties' tax dispute.

A. Creation And Initial Funding

William Fielding is the current trustee of the four appellant Trusts. Each was created by an irrevocable agreement ("Trust Agreements") dated June 25, 2009, between Reid V. MacDonald ("Grantor") and Edmund B. MacDonald, Jr., as trustee.[3] Laura Carlson, a Minneapolis attorney, represented Grantor in drafting the trust Agreements.[4] Grantor was domiciled in Minnesota during 2009, when the Trusts were created, and at all times since 2009.[5] The Trusts' current mailing address is that of Mr. Fielding, in Johnson City, Texas.[6]

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[3] Stip. ¶ 2. The Trust Agreements are Exhibits J9 to J12.

[4] Stip. ¶ 4.

[5] Stip. ¶ 3.

[6] Stip. ¶ 1.

Approximately two weeks after creating the Trusts, by means of a stock-transfer certificate dated July 9, 2009, Grantor funded each trust with 6,021 shares of nonvoting common stock in Faribault Foods, Inc. ("FFI"), a Minnesota Subchapter S corporation.[7] FFI recorded the stock transfer as effective August 1, 2009.[8] Edmund MacDonald, in his capacity as trustee, thus acquired possession and legal title of trust assets, which passed to his successor trustees.[9]

B. Change In Status For Tax Purposes

From June 25, 2009, through December 31, 2011, the Trusts were "grantor type trusts" for Minnesota income tax purposes, because Grantor retained a power to exchange personal assets for Trust assets of equivalent value.[10] For this period, trust income was treated as income to Grantor, and was taxable as such. On December 31, 2011, however, Grantor signed for each Trust a release of his power to exchange assets.[11] The Trusts thus became "resident trusts" under

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[7] Stip. ¶ 5.

[8] Stip. ¶ 5.

[9] *See, e.g.,* Ex. J09 at FIE000001, FIE000023.

[10] Stip. ¶ 6. *See* Minn. Stat. § 290.01, subd. 7b(a) (2016) ("The term 'grantor type trust' means a trust where the income or gains of the trust are taxable to the grantor or others treated as substantial owners under sections 671 to 678 of the Internal Revenue Code.").

[11] Stip. ¶ 7.

Minnesota law,[12] and were thereafter treated as entities themselves subject to state income tax.

C. Trustees And Trust Administration

The Trusts had only one trustee at any time, who was the same for each Trust.[13] At no time was any trustee domiciled in Minnesota.[14] Edmund MacDonald, a California domiciliary, was the initial trustee, serving from August 1, 2009, through December 31, 2011.[15]

Katherine A. Boone was trustee between January 1, 2012, and July 24, 2014.[16] She was a Colorado domiciliary for the entire period, and never traveled to Minnesota.[17] During 2014, Boone made all discretionary decisions concerning distributions to beneficiaries and investment of trust assets while in Colorado.[18]

[12] Stip. ¶ 8. *See* Minn. Stat. § 290.01, subd. 7b(a)(2) (defining "[r]esident trust" as "an irrevocable trust, the grantor of which was domiciled in this state at the time the trust became irrevocable," and further providing that "a trust is considered irrevocable to the extent the grantor is not treated as the owner thereof under sections 671 to 678 of the Internal Revenue Code").

[13] Stip. ¶ 14.

[14] Stip. ¶ 14.

[15] Stip. ¶ 15; Ex. J13 (MacDonald resignation).

[16] Stip. ¶¶ 16, 18; Exs. J14 to J15 (Boone appointment and acceptance).

[17] Stip. ¶ 18.

[18] Stip. ¶¶ 102-03.

Ms. Boone resigned and appointed Mr. Fielding trustee, effective July 24, 2014.[19] He continues to serve as trustee of the Trusts, and has been a Texas domiciliary throughout his service.[20] Fielding has never travelled to Minnesota on trust-related business.[21] During 2014, Fielding made all discretionary decisions concerning distributions to beneficiaries and investment of trust assets while in Texas.[22]

During 2014, Ms. Boone and Mr. Fielding maintained records of trust assets and income.[23] Boone "kept bank account statements and income tax returns in Colorado";[24] Fielding "kept bank account statements, investment information and account statements, income tax returns and information about the proposed sale of FFI in Texas."[25] Although attorney Carlson initially maintained the original Trust Agreements in Minnesota, she mailed them to Fielding on September 19, 2014.[26] In their capacity as trustees of the Trusts, the trustees "have not been plaintiffs or defendants in any legal action filed in the courts of Minnesota or of

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[19] Stip. ¶¶ 17, 19; Ex. J16 (Boone resignations; Fielding appointments and acceptances).

[20] Stip. ¶ 19.

[21] Stip. ¶ 20.

[22] Stip. ¶¶ 102-03.

[23] Stip. ¶ 105.

[24] Stip. ¶ 105.

[25] Stip. ¶ 105.

[26] Stip. ¶ 107.

any other state, except for the instant cases pending in the Minnesota Tax Court."[27]

D. Beneficiaries

The primary beneficiary of the Maria Trust is Grantor's daughter, Maria V. MacDonald. Maria was born in Minnesota in 1985. She was domiciled in California during 2014, and remains a California domiciliary. Maria filed a California resident income tax return for 2014. She did not maintain a place of abode in Minnesota at any time during 2014.[28]

The primary beneficiary of the Catherine Trust is Grantor's daughter, Catherine Gray MacDonald. Catherine was born in Minnesota in 1986. She was domiciled in New York during 2014. Catherine moved to California in 2015, and remains a California domiciliary. Catherine filed a New York resident income tax return for 2014. She did not maintain a place of abode in Minnesota at any time during 2014.[29]

The primary beneficiary of the Laura Trust is Grantor's daughter, Laura Reid MacDonald. Laura was born in Minnesota in 1988. She was domiciled in New York during 2014. Laura moved to California in 2015, and remains a California domiciliary. Laura filed a New York resident income tax return for 2014. She did not maintain a place of abode in Minnesota at any time during 2014.[30]

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[27] Stip. ¶ 104.

[28] Stip. ¶ 21.

[29] Stip. ¶ 22.

[30] Stip. ¶ 23.

The primary beneficiary of the Vandever Trust is Grantor's son, Vandever R. MacDonald. Vandever was born in Minnesota in 1993. He was domiciled in Minnesota during 2014, but attended college in New York. Vandever filed a Minnesota resident income tax return for 2014.[31]

E. Additional Trust Assets

During 2011, each Trust acquired 16,223 additional shares of nonvoting common stock in FFI.[32] Consequently, between December 31, 2011, and August 1, 2014, when the stock was sold, each Trust owned 22,244 shares in FFI.[33] The only other asset in each Trust, prior to sale of the FFI stock, was cash held in a Wells Fargo checking account.[34]

F. Sale Of The FFI Stock

Each Trust Agreement recited that Grantor assigned, transferred, and delivered to the trustee certain properties, and provided that "[t]he legal title to the trust property shall be and remain vested in the Trustee and any successor ...."[35] The trustee of each Trust has the power "[t]o sell ... any or all of the properties of the Trust Estate at such prices, on such terms, to such persons, in such portions, and in such manner as the Trustee may in each case deem proper

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[31] Stip. ¶ 24.

[32] Stip. ¶ 25.

[33] Stip. ¶25.

[34] Stip. ¶ 26; Exs. J17A to J20B (Trusts' checking account statements).

[35] *See, e.g.,* Ex. J09 at FIE000001, FIE000023.

and advisable."[36] In July 2014, Mr. Fielding reviewed information about a proposed sale of FFI stock to La Costeña USA, Inc. He also participated in a conference call of shareholders on July 24, 2014, to discuss the possible transaction.[37] Fielding exercised his discretion to sell the FFI stock held by each Trust to La Costeña on August 1, 2014.[38] All other FFI shareholders likewise sold their stock that same day.[39]

There were 526,310.80 shares of FFI stock outstanding at the time of sale, of which 47,846.40 were shares of voting common stock and 478,464.40 were shares of nonvoting common stock. All outstanding shares received the same price. Each Trust owned 22,244 shares of nonvoting common stock in FFI, and was thus entitled to receive 4.226 percent of the sale proceeds (22,244/526,310.80).[40]

G. Disposition Of Sale Proceeds

Each Trust's Wells Fargo checking account statement reflects a substantial deposit in August 2014—proceeds received at the closing of the FFI stock sale. The bank statements likewise reflect that each Trust received two lesser deferred payments, one in September 2014 and one in December 2014.[41]

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[36] Stip. ¶ 63 (quoting section 5.1(4) of each Trust Agreement).

[37] Stip. ¶ 62.

[38] Stip. ¶63.

[39] Stip. ¶ 64.

[40] Stip. ¶ 65.

[41] Stip. ¶ 31.

In October 2014, Mr. Fielding entered into an Asset Management Agreement for each Trust with Wells Fargo.[42] Fielding gave Wells Fargo full discretion to manage (purchase, sell, or retain) trust assets in accordance with the Investment Policy Statement for each account.[43] On October 20, 2014, Fielding approved the transfer of funds from each Trust's checking account to its new investment account.[44] Wells Fargo managed the Trusts' investment accounts from its offices in San Francisco, California.[45] The Wells Fargo checking and investment account statements are the only records of trust assets and income during 2014 (other than tax returns).[46]

H. Distributions To Beneficiaries During 2014

Under the Trust Agreements, the trustee "may distribute to or for the benefit of the Primary Beneficiary such sum or sums from either the net income from or the principal of such separate trust, including the whole thereof, as the Trustee, in the exercise of the Trustee's discretion, may deem necessary or advisable from time to time."[47] Exercising this discretion, the trustees (first Ms. Boone, and then Mr. Fielding) made both periodic and one-time distributions during 2014. Maria, Catherine, and Laura

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[42] Stip. ¶ 32; Exs. J21 to J24 (Asset Management Agreements).

[43] Stip. ¶ 32.

[44] Stip. ¶ 37.

[45] Stip. ¶ 38.

[46] Stip. ¶ 43; Exs. J25 to J28 (Trusts' 2014 investment account statements).

[47] Stip. ¶ 44 (quoting section 4.2(2) of each Trust Agreement).

each received a monthly distribution for eleven months of 2014;[48] Vandever received one for all twelve months.[49] Maira also received a one-time distribution during October (to assist in the purchase of a residence).[50]

I. Income Tax Reporting

Each Trust timely filed a 2014 Minnesota income tax return as a Minnesota "resident trust" under Minn. Stat. § 290.01, subd. 7b(a)(2), paid the reported tax under protest, and included a statement asserting that the statutory definition was unconstitutional.[51] Each Trust next filed an amended 2014 Minnesota return prepared *without* treating itself as a Minnesota "resident trust."[52] The amended returns excluded from each Trust's taxable income: (1) gain from the 2014 FFI stock sale; and (2) income from the Trust's Wells Fargo investment account (administered in California). Briefly, the Trusts argued that the stock and investment accounts are intangible personal property located outside of Minnesota, and that Minnesota may not lawfully tax income or gains attributable to those assets. On this basis, each of three Trusts requested a substantial refund.[53]

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[48] Stip. ¶ 45, 48, 52.

[49] Stip. ¶ 52.

[50] Stip. ¶¶ 45-46.

[51] Stip. ¶ 88; Exs. J49 to J52 (Trusts' 2014 Minnesota income tax returns).

[52] Stip. ¶ 93; Exs. J53 to 56 (Trusts' amended 2014 Minnesota income tax returns).

[53] Stip. ¶¶ 94-97.

In addition to filing a Minnesota income tax return, each Trust also filed state income tax returns in Arizona, California, Colorado, and Illinois.[54]

II. GENERAL PRINCIPLES

The Trusts ask us to rule as a matter of law that Minnesota's definition of "resident trust," as applied to them, violates the due process provisions of the Minnesota and United States constitutions and the Commerce Clause of the Federal Constitution. The Commissioner asks us to rule as a matter of law that the challenged statute is constitutional as applied to the Trusts.

Summary judgment shall be rendered if the pleadings, the record in the case, and any supporting affidavits show that there is no genuine issue as to any material fact and that a party is entitled to judgment as a matter of law. Minn. R. Civ. P. 56.03; *DLH, Inc. v. Russ,* 566 N.W.2d 60, 69 (Minn. 1997). When, as here, parties file cross-motions for summary judgment, they tacitly agree that there are no genuine issues of material fact. *Am. Family Mut. Ins. Co. v. Thiem,* 503 N.W.2d 789, 790 (Minn. 1993). Summary judgment is a suitable vehicle for addressing the application of law to undisputed facts. *See A. J. Chromy Constr. Co. v. Commercial Mech. Serv., Inc.,* 260 N.W.2d 579, 581 (Minn. 1977).

Minnesota statutes are presumed constitutional. *Kimberly-Clark Corp. & Subsidiaries v. Comm'r of Revenue,* 880 N.W.2d 844, 848 (Minn. 2016). The

[54] Stip. ¶¶ 98-101; Exs. J57 to J73 (Trusts' original and amended state income tax returns filed in states other than Minnesota).

Minnesota Supreme Court has emphasized: "We exercise our power to declare a statute unconstitutional with extreme caution and only when absolutely necessary." *Luther v. Comm'r of Revenue,* 588 N.W.2d 502, 508 (Minn. 1999). "Accordingly, [a court] will uphold a statute unless the challenging party demonstrates that it is unconstitutional beyond a reasonable doubt." *Caterpillar, Inc. v. Comm'r of Revenue,* 568 N.W.2d 695, 697-98 (Minn. 1997).[55]

III. CHALLENGED STATUTE

Minnesota Statutes section 290.01, subdivision 7b, defines "resident trust" for state income tax purposes, and provides, in part:

> (a) Resident trust means a trust, except a grantor type trust, which either (1) was created by a will of a decedent who at death was domiciled in this state or (2) is an irrevocable trust, the grantor of which was domiciled in this state at the time the trust became irrevocable.

Minn. Stat. § 290.01, subd. 7b(a). Expressly excluded from this definition is a "grantor type trust," as to

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[55] The Legislature created the tax court as an administrative agency of the executive branch. *See* Minn. Stat. § 271.01, subd. 1 (2016). Generally, our jurisdiction is limited to "questions of law and fact arising under the tax laws of the state." Minn. Stat. § 271.01, subd. 5 (2016). When, however, a case first comes to us by transfer from the district court, or when a case is transferred to, and back again from, the district court (a procedure known as the "Erie Shuffle"), we acquire jurisdiction to decide constitutional matters. *See Wilson v. Comm 'r of Revenue,* 619 N.W.2d 194, 199-200 (Minn. 2000). Because an Erie Shuffle was completed in each case, we have jurisdiction to decide the Trusts' constitutional challenges.

which "the income or gains of the trust *are taxable to the grantor* [rather than to the trust itself] ... under sections 671 to 678 of the Internal Revenue Code." *Id.* (emphasis added). Correspondingly, a trust is a "resident trust" "to the extent the grantor *is not treated as the owner thereof* under sections 671 to 678 .... " *Id.* (emphasis added). To precisely this latter extent, the trust itself—rather than the grantor—is liable for tax on trust income or gains. These cases involve irrevocable *inter vivos* trusts (rather than testamentary trusts "created by a will of a decedent").

The foregoing definition of "resident trust" does *not* apply to all irrevocable *inter vivos* trusts. Instead, it applies only "to trusts ... that became irrevocable after December 31, 1995, or are first administered in Minnesota after December 31, 1995." Minn. Stat. § 290.01, subd. 7b(a). A second definition of "resident trust" governs trusts "that are not governed under paragraph (a)." Minn. Stat. § 290.01, subd. 7b(b). This second definition provides:

> A trust, except a grantor type trust, is a resident trust only if two or more of the following conditions are satisfied:
>
> (1) a majority of the discretionary decisions of the trustees relative to the investment of trust assets are made in Minnesota;
>
> (2) a majority of the discretionary decisions of the trustees relative to the distributions of trust income and principal are made in Minnesota;
>
> (3) the official books and records of the trust, consisting of the original minutes of trustee

> meetings and the original trust instruments, are located in Minnesota.

Minn. Stat. § 290.01, subd. 7b(b). A separate subdivision addresses how to apply these nexus criteria when a trustee delegates decision-making authority. *See* Minn. Stat. § 290.01, subd. 7b(c).

IV. DUE PROCESS CONSTRAINTS ON STATE TAXATION OF INCOME

The Minnesota and United States constitutions both provide that no person shall be deprived "of life, liberty, or property without due process of law." Minn. Const. art. I, § 7; U.S. Const. amend. XIV, § 1. With respect to state taxation, due process imposes two constraints. First, there must be "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." *Miller Bros. Co. v. Maryland,* 347 U.S. 340, 344-45 (1954). Second, "the income attributed to the State for tax purposes must be rationally related to 'values connected with the taxing State.'" *Moorman Mfg. Co. v. Bair,* 437 U.S. 267, 273 (1978) (citation omitted).

A. Two-Component Nexus Inquiry

Due process nexus actually "embodies two discrete inquiries: first, is there a minimum connection with (and hence, jurisdiction over) the taxpayer; second, is there a minimum connection with (and hence, jurisdiction over) the activity the state seeks to tax." Walter Hellerstein, *State Taxation* ¶ 6.02 (3d ed. 2017) [hereinafter Hellerstein] (footnote omitted). The first inquiry involves "whether a state has a sufficient connection or 'nexus' with the taxpayer ... to permit the state to compel the taxpayer ... to comply with the state's tax obligations." *Id.,* ¶ 6.01[1]. "These are essentially questions of personal or *in personam* jurisdiction." *Id.; see also Allied-Signal, Inc. v. Dir., Div. of Taxation,* 504 U.S. 768, 778 (1992) ("The constitutional question in a case such as *Quill Corp.* is whether the State has the authority to tax the corporation at all."). The second (but discrete) inquiry "may involve questions of whether a state has power over the subject matter of the tax." Hellerstein ¶ 6.01[2]. As the Supreme Court has explained, "in the case of a tax on an activity, there must be a connection to the activity itself, rather than a connection only to the actor the State seeks to tax." *Allied-Signal,* 504 U.S. at 778. "Failure to distinguish clearly between these two aspects of taxing jurisdiction can confuse the proper understanding and analysis of jurisdiction-to-tax questions." Hellerstein ¶ 6.01.[56]

1. Personal Jurisdiction

A state's jurisdiction to tax a person is evaluated under familiar due process principles. *Quill Corp. v. North Dakota,* 504 U.S. 298, 307-08, 312 (1992). Applying these principles, the Supreme Court rejected Quill's claim that North Dakota lacked jurisdiction to require Quill to collect and remit North Dakota use tax. *Id.* at 303. Quill sold office equipment and supplies to North Dakota customers, soliciting business through catalogs and flyers, advertisements in national periodicals, and telephone calls. *Id.* Quill had no

[56] *See also* Hellerstein ¶ 6.04 (reiterating that personal and subject matter jurisdiction are "two discrete inquiries" and cautioning that "it is important to address them separately because failing to distinguish between the precise jurisdictional questions under consideration can lead to confusion and unsound analysis").

employees in North Dakota, owned no tangible property there, and delivered all merchandise to customers by common carrier. *Id.* Although Quill had no physical presence in North Dakota, the Supreme Court sustained North Dakota's personal jurisdiction over Quill:

> [T]here is no question that Quill has purposefully directed its activities at North Dakota residents, that the magnitude of those contacts is more than sufficient for due process purposes, and that the use tax is related to the benefits Quill receives from access to the State. We therefore agree with the North Dakota Supreme Court's conclusion that the Due Process Clause does not bar enforcement of that State's use tax against Quill.

Id. at 308.

2. Subject Matter Jurisdiction

If a state has personal jurisdiction, the next question is whether it also has subject matter jurisdiction. In this case, we deal with the taxation of income. "There are two fundamental, but alternative, bases for state power to tax income: residence and source." Hellerstein ¶ 6.04.

a. Residency

The Supreme Court has long held that residency confers jurisdiction to tax *all* of a taxpayer's income *without regard to source. See, e.g., New York ex rel. Cohn v. Graves,* 300 U.S. 308 (1937). In *Graves,* a New York resident challenged that state's jurisdiction to tax "income [she] received from rents of land located without the state [in New Jersey] and from interest on bonds physically without the state and secured by mortgages upon lands similarly situated." *Id.* at 310-12. The Court rejected this challenge:

> That the receipt of income by a resident of the territory of a taxing sovereignty is a taxable event is universally recognized. Domicil itself affords a basis for such taxation. ... A tax measured by the net income of residents ... is founded upon the protection afforded by the state to the recipient of the income in his person, in his right to receive the income and in his enjoyment of it when received. These are rights and privileges which attach to domicil within the state.

Id. at 312-13. The Court emphasized that this conclusion was not "affected by the character of the source from which the income is derived," commenting that "[a] state may tax its residents upon net income from a business whose physical assets, located wholly without the state, are beyond its taxing power." *Id.* at 313; *see also Oklahoma Tax Comm'n v. Chickasaw Nation,* 515 U.S. 450, 462-63 (1995) (applying the "well-established principle of interstate and international taxation—namely, that a jurisdiction ... may tax *all* of the income of its residents, even income earned outside the taxing jurisdiction"). Residency, then, confers subject matter jurisdiction over a person's worldwide income *without regard to source.*[57]

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[57] Minnesota taxes all of a resident individual's income. *See* Minn. Stat. § 290.014, subd. 1 (2016) ("All net income of a resident individual is subject to tax under this chapter."); Minn. Stat. § 290.17, subd. 1 (a) (2016) ("The income of resident individuals is

b. Source

For nonresident taxpayers, in contrast, subject matter jurisdiction must be established for each source of income. *See, e.g., Shaffer v. Carter,* 252 U.S. 37, 57 (1920). In *Shaffer,* the Court contrasted a state's taxing power over residents and nonresidents, respectively:

> As to residents [the state] may, and does, exert its taxing power over their income from all sources, whether within or without the state . . . . As to nonresidents, the jurisdiction extends only to their property owned within the state and their business, trade, or profession carried on therein, and the tax is only on such income as is derived from those sources.

Id.; see also Chickasaw Nation, 515 U.S. at 463 n.11 (noting that for nonresident taxpayers "jurisdictions generally may tax only income earned within the jurisdiction"); *Luther,* 588 N.W.2d at 507 ("The state taxes the income of nonresidents only to the extent that income is derived from activities within Minnesota."). Thus, even when a state has personal jurisdiction over a nonresident taxpayer, the state may tax only income derived from in-state sources—*not* the taxpayer's worldwide income. "The bedrock constitutional principle that a state may not tax activities with which it lacks a concrete connection generally confines the exercise of a state's tax power to activities conducted within its borders." Hellerstein ¶ 8.07.

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not subject to allocation outside this state."); *Luther,* 588 N.W.2d at 507 ("If a taxpayer is a Minnesota 'resident,' Minnesota taxes her worldwide net income.").

The more constrained taxing power arising from the source justification is well illustrated by two aspects of business taxation: apportionment and tax-base limitation. Under the source justification, when a nonresident taxpayer's business is carried on partly within and partly without a state, the state may tax income derived only from the business' local activities. This can be achieved by "separate geographic accounting." *See Mobil Oil Corp. v. Comm'r of Taxes of Vermont,* 445 U.S. 425, 438 (1980).[58] The Supreme Court has long held, however, that "a State need not attempt to isolate the intrastate income-producing activities from the rest of the business; it may tax an apportioned sum of the corporation's multistate business if the business is unitary." *Allied-Signal,* 504 U.S. at 772. The Court has thus approved apportionment as an adequate method for establishing the amount of income derived from a multistate business's in-state activities. *Moorman,* 437 U.S. at 273 & n.6 (commenting that apportionment "is employed as a rough approximation of a corporation's income that is reasonably related to the activities conducted within the taxing State").

The source justification likewise prohibits a state from including in the apportionable tax base income from property or activities unrelated to a nonresident taxpayer's in-state business. In *Allied-Signal,* a nondomiciliary corporation sought an income tax refund because New Jersey had included in its

[58] "Separate accounting is a method for determining the geographic source of a taxpayer's income through segregation of the profits attributable to a state through identification of state specific receipts, costs, and expenses from the taxpayer's books and records." Hellerstein ¶ 8.03.

apportionable tax base the gain Allied-Signal had realized on its sale of stock in a separate corporation (ASARCO, Inc.), one unrelated to Allied-Signal's business conducted partly within New Jersey. *Allied-Signal,* 504 U.S. at 773-76.

The Court ruled that New Jersey lacked jurisdiction to tax Allied-Signal's gain on the ASARCO stock sale. *Id.* at 790. Based on the stipulated facts, the Court easily concluded that the two entities—Bendix and ASARCO—were *not* engaged in a unitary business. *Id.* at 774-75, 788. It also concluded that Allied-Signal's investment in ASARCO stock had no operational role in Allied-Signal's business operations. *Id.* at 788-89.

The Court agreed with certain New Jersey *amici curiae* "that the Constitution does not require a unitary business relation between the payor and the payee in order for a State to apportion the income the payee corporation receives from an investment in the payor." *Id.* at 786. "What is required instead is that the capital transaction serve an operational rather than an investment function." *Id.* at 787.

> Hence, for example, a State may include within the apportionable income of a nondomiciliary corporation the interest earned on short-term deposits in a bank located in another State if that income forms part of the working capital of the corporation's unitary business, notwithstanding the absence of a unitary relationship between the corporation and the bank.

Id. at 787-88.

In sum, although the Supreme Court's contemporary due process jurisprudence "rejects a rigid, formalistic definition of minimum connection," the Court has not "abandoned the requirement that, in the case of a tax on an activity, there must be a connection to the activity itself, rather than a connection only to the actor the State seeks to tax." *Id.* at 778. Subject matter jurisdiction—the need to establish that income was derived from in-state activity—thus remains a significant limitation upon a state's power to tax nonresident taxpayers.[59]

B. Relation Between Income Taxed And Benefits Conferred

The second requirement of due process is that the "income attributed to the State for tax purposes must be rationally related to 'values connected with the taxing State.'" *Moorman,* 437 U.S. at 273 (citation omitted). This requirement is violated when a state taxes "extraterritorial values wholly unrelated" to a taxpayer's in-state business. *F. W. Woolworth Co. v. Taxation & Revenue Dep't of State of N. M,* 458 U.S.

[59] Under Minnesota law, capital transactions that serve solely an investment function fall under the definition of "nonbusiness income," and must be assigned to the taxpayer's domicile:

> Nonbusiness income is income of the trade or business that cannot be apportioned by this state because of the United States Constitution or the Constitution of the state of Minnesota and includes income that cannot constitutionally be apportioned to this state because it is derived from a capital transaction that solely serves an investment function. Nonbusiness income must be allocated ....

Minn. Stat. § 290.17, subd. 6 (2016).

354, 372 (1982) (citation omitted); *Hans Rees' Sons v. North Carolina ex rel. Maxwell,* 283 U.S. 123, 134, 135 (1931) (reversing an assessment where the state apportionment formula "operate[d] so as to reach profits which [were] in no just sense attributable to transactions within its jurisdiction," and thus attributed to the taxpayer "income out of all appropriate proportion to the business transacted ... in that state"). The requirement is satisfied, on the other hand, when "the tax is fairly apportioned to the commerce carried on within the State." *Ott v. Miss. Valley Barge Line Co.,* 336 U.S. 169, 174 (1949); *see also Container Corp. v. Franchise Tax Bd.,* 463 U.S. 159, 169 (1983) (holding that the Due Process Clause requires an apportionment formula to be "fair").

V. THE TRUSTS' DUE PROCESS CLAIM

The Trusts claim that section 290.01, subdivision 7b(a)(2), violates due process as applied to them because under that provision, "the Trusts will be classified as resident trusts, and be subject to Minnesota income tax on income and gains from intangibles, for as long as the Trusts exist (probably decades) based *solely* on the historic fact that Reid MacDonald was domiciled in Minnesota on December 31, 2011."[60] According to the Trusts, this single "historical fact" is not an adequate basis to designate a taxpayer a "resident trust," and thus to tax its worldwide income:

> Minnesota cannot subject the Trusts to income tax on 100 percent of their investment income by

[60] Appellants' Mem. Supp. Summ. J. 2-3 (filed Jan. 27, 2017) (footnote omitted).

> classifying them as "resident trusts," a classification that depends entirely on the domicile of the grantor on December 31, 2011, the date the Trusts were deemed to be irrevocable. The vestigial connection of the grantor is not a permissible basis for classifying a trust as a resident.[61]

Specifically, the Trusts allege that Minnesota had no authority to tax them on: (1) gains from the 2014 sale of FFI stock (intangible assets possessed by trustees domiciled outside of Minnesota); or (2) income from the Trusts' Wells Fargo investment accounts (administered in California), because these amounts were "[i]ncome or gains from intangible personal property not employed in the business of the recipient." Minn. Stat. § 290.17, subd. 2(c). They ask us to rule as a matter of law that section 290.01, subdivision 7b(a)(2) is unconstitutional as applied to them, and to reverse the Commissioner's orders denying their refund claims.[62]

Alleging that "[t]he Trusts seek to curtail Minnesota's power to define trust residency,"[63] the Commissioner argues that the Trusts "cannot meet their burden to prove a constitutional violation beyond a reasonable doubt."[64] In a section titled "The Trusts Have Many Links To Minnesota," the Commissioner argues that the State "has extended a host of benefits

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[61] Appellants' Mem. Supp. Summ. J. 32.

[62] Appellants' Mem. Supp. Summ. J. 43.

[63] Appellee's Mem. Supp. Summ. J. 11 (filed Jan. 27, 2017).

[64] Appellee's Mem. Supp. Summ. J. 1.

to the Trusts in this case."[65] Specifically, the Commissioner points to the following:

- "All four Trusts were created by Grantor MacDonald, a Minnesota domiciliary";
- "All four original trust documents were drafted by [a] Minnesota attorney ... , and they state they are to be interpreted according to the laws of the State of Minnesota";
- "From the time of the Trusts' creation until late 2014, the trust documents were kept in Minnesota";
- "Vandever Macdonald [sic], one of the four primary beneficiaries, was domiciled in Minnesota in 2014"; and
- "[T]he Trusts' primary trust asset and source of income during 2014 was stock in FFI, a closely held S-Corporation which was incorporated in the State of Minnesota and has always been headquartered in Minnesota."[66].

Citing these and other factors, the Commissioner argues that foreign cases analyzing due process

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[65] Appellee's Mem. Supp. Summ. J. 8.

[66] Appellee's Mem. Supp. Summ. J. 8. *See also id.* at 22 ("The State's justification for taxing the Trusts as residents ... is that the State has provided a wide array of benefits to the Trusts as the state of their creation, the state of incorporation of FFI, and the state of domicile for Grantor MacDonald and beneficiary Vandever.").

challenges to the taxation of trusts "confirm that Minnesota is well within constitutional bounds in taxing the Trusts in this case."[67] The Commissioner thus asks us to reject the Trusts' due process challenge and to affirm her orders.[68]

The Trusts rejoin that the Commissioner misstates the issue by framing it as whether Minnesota has power to tax the Trusts (in some way): "The issue is whether Minnesota can tax the Trusts *as resident trusts."*[69] They explain: "Here, the Commissioner does not want to tax an apportioned share of the gain from selling FFI stock; she wants to tax 100 percent of that gain .... [S]he also wants to tax 100 percent of non-FFI intangible income (including dividends from mutual funds). In other words, she wants to tax the Trusts as residents of Minnesota."[70] Then, responding to the Commissioner's list of benefits allegedly conferred on them, the Trusts argue: "The Court should not supplement the statutory language by adding factors to the one factor specified in the statute for classifying an inter vivos trust as a resident trust: the historical domicile of the grantor."[71]

VI. ANALYSIS

Before proceeding, we must resolve two preliminary questions arising from the parties' arguments, as just

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[67] Appellee's Mem. Supp. Summ. J. 15-20.

[68] Appellee's Mem. Supp. Summ. J. 1, 25.

[69] Appellants' Reply Mem. 1 (filed Feb. 17, 2017) (emphasis added).

[70] Appellants' Reply Mem. 2.

[71] Appellants' Reply Mem. 2 (sentence capitalization modified).

summarized: the issue presented, and the factors upon which we may rely in evaluating due process connection.

A. Issue Presented

We think the issue presented is: Whether, for due process purposes, the domicile of the grantor alone is a sufficient connection with Minnesota to justify taxing the Trusts *as residents* (that is, on a tax base that includes intangible personal property *not* related to Minnesota). We agree with the Trusts, in other words, that the issue is not simply whether the State has personal jurisdiction to tax the Trusts. This conclusion is supported by several considerations.

First, the parties have stipulated "that the Trusts are Minnesota 'resident trusts' as that term is defined in Minn. Stat. § 290.01, subd. (7b)(a)(2)."[72] Second, it is undisputed that Minnesota taxed the Trusts *as residents.* Pursuant to section 290.17, subdivision 2(c), Minnesota *assigned to itself* "income or gains from intangible personal property not employed in the business of" the Trusts.[73] Referring to the Trusts, the Commissioner's opening submission states: "They were taxed on this gain [from the FFI stock sale] as resident trusts."[74] Finally, the Trusts do *not* dispute that Minnesota properly taxed them—as shareholders of a Subchapter S corporation generating income in Minnesota—on operating income arising from FFI' s in-

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[72] Stip. ¶ 8.

[73] Appellee's Mem. Supp. Summ. J. 9.

[74] Appellee's Mem. Supp. Summ. J. 1.

state business activities.[75] Instead, their challenge pertains to the State's taxation of gains from the sale of FFI stock held by the trustee outside of Minnesota.[76] The question is thus whether Minnesota may tax the Trusts *as residents,* on gains from the sale of intangible assets not related to Minnesota.[77]

B. Scope Of The Court's Due Process Connection Inquiry

We must next determine the proper scope of our due process connection inquiry. The Trusts argue that we should not "supplement the statutory language [of section 290.01, subdivision 7b(a)(2)] by adding factors to the one factor specified in the statute for classifying an inter vivos trust as a resident trust: the historical domicile of the grantor."[78] The Trusts thus argue that

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[75] Appellants' Mem. Supp. Summ. J. 2 n.2, 17 & n.19.

[76] Gain on the sale of S corporation stock is allocable to Minnesota to the extent provided by Minn. Stat. § 290.17. *See* Minn. Stat. § 290.014, subd. 3(1) (2016). Section 290.17 provides, in part, that "[i]ncome or gains from intangible personal property not employed in the business of the recipient of the income or gains *must be assigned to this state if the recipient of the income or gains is ... a resident trust.*" Minn. Stat. § 290.17, subd. 2(c) (2016) (emphasis added). For a nonresident trust, in contrast, gains from intangible personal property not employed in the taxpayer's trade or business "shall be assigned to the taxpayer's domicile." *Id.,* subd. 2(e).

[77] Under the Trust Agreements, the trustee has possession and legal title of trust assets. *See, e.g.,* Ex. J9 at FIE000001, FIE000023. Ms. Boone, who was trustee from January 1 through July 24, 2014, was a Colorado domiciliary. Stip. ¶ 18. Mr. Fielding, who was trustee from July 24 through December 31, 2014, was a Texas domiciliary. Stip. ¶ 19.

[78] Appellants' Reply Mem. 2 (sentence capitalization modified).

we should determine whether the grantor's domicile at the time the Trusts became irrevocable *alone* can justify taxing the Trusts as residents. The Commissioner, on the other hand, contends that we should consider "all the contacts between Minnesota and the Trusts" when analyzing the Trusts' as-applied due process challenge.[79]

We agree with the Commissioner that as-applied challenges are analyzed under all the relevant circumstances. *See, e.g., Rew v. Bergstrom,* 845 N.W.2d 764, 780 (Minn. 2014). The Commissioner simply *assumes,* however, that all the contacts between Minnesota and the Trusts are relevant when applying section 290.01, subdivision 7b(a)(2). We cannot agree.

When evaluating a constitutional challenge to a statute, a court must first determine the statute's meaning; must next apply the statute in accordance with legislative intent; and only then must decide whether the statute, as applied, violates the constitution. *State v. Muccio,* 890 N.W.2d 914, 919-20 (Minn. 2017) (so proceeding); *Wuertz v. Garvey,* 287 Minn. 353, 354-55, 178 N.W.2d 630, 631-32 (1970) (same). Statutory interpretation and application thus precede constitutional adjudication. *Muccio,* 890 N.W.2d at 920. When considering the Trusts' as-applied challenge to section 290.01, subdivision 7b(a)(2), therefore, we must identify the specific circumstances upon which the Legislature intended to base residency for purposes of that provision.

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[79] Appellee's Reply Mem. 2 (filed Feb. 17, 2017) (citing *Rew v. Bergstrom,* 845 N.W.2d 764, 780 (Minn. 2014)).

C. Interpretation Of Section 290.01, Subdivision 7b

"The object of all interpretation and construction of laws is to ascertain and effectuate the intention of the legislature." Minn. Stat. § 645.16. (2016). Legislative intent is determined "primarily from the language of the statute itself." *Brayton v. Pawlenty,* 781 N.W.2d 357, 363 (Minn. 2010) (quoting *Gleason v. Geary,* 214 Minn. 499, 516, 8 N.W.2d 808, 816 (1943)). When initially ascertaining the meaning of a particular provision, a court considers related provisions: "It is a cardinal rule of statutory construction that a particular provision of a statute cannot be read out of context but must be taken together with other related provisions *to determine its meaning." Kollodge v. F. & L. Appliances, Inc.,* 248 Minn. 357, 360, 80 N.W.2d 62, 64 (1956) (emphasis added). Courts thus "interpret each section in light of the surrounding sections to avoid conflicting interpretations," *Am. Family Ins. Grp. v. Schroedl,* 616 N.W.2d 273, 277 (Minn. 2000), and to "harmonize and give effect to all its parts," *Van Asperen v. Darling Olds, Inc.,* 254 Minn. 62, 73-74, 93 N.W.2d 690, 698 (1958). "When the words of a law in their application to an existing situation are clear and free from all ambiguity, the letter of the law shall not be disregarded under the pretext of pursuing the spirit." Minn. Stat. § 645.16.

The challenged statute contains two separate definitions of "resident trust." The subdivision 7b(a)(2) definition specifies a single criterion for determining the residency of an *inter vivos* trust: the domicile of the grantor when the trust became irrevocable. Minn. Stat. § 290.01, subd. 7b(a)(2). Under the plain meaning of this definition, residency is determined by a single, historical fact.

The subdivision 7b(b) definition, in contrast, enumerates several criteria for determining residency, all focusing on whether a trust is administered in Minnesota. Minn. Stat. § 290.01, subd. 7b(b). More specifically, residency under this definition turns on whether certain discretionary investment and distribution decisions "are made" in Minnesota, and whether certain trust-related documents "are located" in Minnesota. Minn. Stat. § 290.01, subd. 7b(b)(1)-(3).[80] For economy, we refer to the subdivision 7b(a) definition as the "grantor-domicile rule," and the subdivision 7b(b) definition as the "Minnesota-nexus rule."

Each rule contains language specifying its intended scope of application. By its express terms, subdivision 7b(a) applies to *inter vivos* trusts "that became irrevocable after December 31, 1995, or are first

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[80] Income tax is imposed on an annual basis. *See* Minn. Stat. § 290.03(3) (2016) (imposing "[a]n annual tax for each taxable year ... upon the taxable income for such year" of "[t]rusts ... however created by residents or non-residents"). Residency is thus determined on an annual basis. *See, e.g., Stelzner v. Comm'r of Revenue,* 621 N.W.2d 736, 739 (Minn. 2001) (upholding the Commissioner's determination "that the Stelzners were nondomiciliary residents of Minnesota for each year of the audit period"). Accordingly, the Legislature's use of the present tense in framing the nexus criteria contained in section 290.01, subdivision 7b(b) indicates its intention to refer to facts in existence during each separate tax year. *Cf. Marks v. Comm'r of Revenue,* 875 N.W.2d 321, 325 (Minn. 2016) (discussing how to apply the State's nondomiciliary resident statute to the facts obtaining during the particular tax year in issue).

administered in Minnesota after December 31, 1995." Minn. Stat. § 290.01, subd. 7b(a). Subdivision 7b(b) applies to trusts "that are not governed under paragraph (a)." Minn. Stat. § 290.01, subd. 7b(b). These complementary scope provisions thus divide all covered trusts into two separate buckets. The grantor-domicile rule applies exclusively to trusts in the first bucket, while the Minnesota-nexus rule applies exclusively to trusts in the second.

Based on the plain meaning of section 290.01, subdivision 7b—particularly when subdivisions 7b(a) and 7b(b) are read together and harmonized—it is clear that the Legislature intended Minnesota's two definitions of "resident trust" to be mutually exclusive, and to apply to two discrete categories of trusts. Accordingly, we conclude that the sole factor upon which the Legislature intended to base residency for purposes of the grantor-domicile rule is the domicile of the grantor at the time a trust became irrevocable.

"When the Legislature's intent is discernible from plain and unambiguous language, statutory construction is neither necessary nor permitted; and courts apply the statute's plain meaning." *State v. Jones,* 848 N.W.2d 528, 535 (Minn. 2014) (citing *Am. Tower, L.P. v. City of Grant,* 636 N.W.2d 309, 312 (Minn. 2001)). Recourse to general nexus factors when applying the grantor-domicile rule would affirmatively contravene the Legislature's clear intention to create two separate rules, based on separate notions (grantor domicile and nexus), applying two separate sets of criteria. Consequently, when analyzing the Trusts' as-applied challenge to the grantor-domicile rule, we will ask whether the domicile of the grantor—standing alone—is a sufficient connection upon which to justify taxing the Trusts as Minnesota residents. *See supra* § VI.A (issue presented). We will not, as the Commissioner requests, consider other (nexus) factors such as the storage in Minnesota of trust instruments or the Minnesota domicile of a beneficiary.[81]

D. Grantor-Domicile As A Basis For Resident Tax Treatment

As previously indicated, due process permits state taxation of two different scopes, based on two discrete justifications, associated with two separate levels of state connection. Hellerstein ¶ 6.04:

Justification	**Connection**	**Scope of Income Taxation**
Residency	Domicile	Worldwide income
Source	Minimum connection	Income from in-state sources only

Here, the State taxed the Trusts *as residents,* on their worldwide income. The Trusts argue that the domicile of the grantor, standing alone, is an insufficient basis to justify that scope of taxation. We thus agree with the Commissioner that the determinative question is whether due process "curtail[s] Minnesota's power to define trust residency."[82] Specifically, it is whether *the domicile of the grantor at the time the trust became irrevocable* is a connection of sufficient substance to replace *the domicile of the taxpayer itself* as a

[81] Appellee's Mem. Supp. Summ. J. 8, 13, 16-18, 25.

[82] Appellee's Mem. Supp. Summ. J. 11.

justification for taxing worldwide income. Reviewing the pertinent authorities, we conclude it is not.[83]

1. *Mercantile-Safe Deposit*

The first is *Mercantile-Safe Deposit* & *Trust Co. v. Murphy,* 19 A.D.2d 765, 242 N.Y.S.2d 26 (1963), *aff'd,* 203 N.E.2d 490 (N.Y. App. Div. 1964). In 1953, the grantor, a New York domiciliary, "transferred and delivered to" the trustee, a Maryland domiciliary, "3500 shares of the capital stock of a certain corporation." *Id.* at 765, 242 N.Y.S.2d at 27. The grantor subsequently "bequeathed cash and securities to an amount exceeding $1,000,000 to the trustee for the uses and purposes of the trust." *Id.* at 765, 242 N.Y.S.2d at 27. The trust indenture provided that upon the grantor's death, his wife would become the trust's income beneficiary, "subject to the power of the trustee in its absolute discretion to withhold and accumulate all or

[83] If due process did not limit the manner in which states define residency—and thus the manner in which they assert authority to tax worldwide income—states could easily circumvent due process limitations upon the source-justification. Under the source-justification, a nonresident who earns income in a state may be taxed on that income (and only that income). Surely, a state could not—simply by expanding its definition of "resident" to include anyone who earned income in the state—suddenly tax that person's worldwide income. *Cf. D.C. v. Chase Manhattan Bank,* 689 A.2d 539, 544 (D.C. 1997) ("The fact that the District calls some entity—be it a trust, individual, or corporation—a 'resident' does not, by itself, give the District any greater power over that entity than it would have in the absence of such a statutory classification."); *Blue v. Dep't of Treasury,* 411, 462 N.W.2d 762, 764-65 (Mich. Ct. App. 1990) (noting that the court was "unpersuaded by [the State's] arguments that the fact that the trust is defined as a resident trust imparts legal protections and jurisdiction" to tax the trust).

any part of the trust income otherwise payable to her and to merge it with the principal of the fund from which it was derived." *Id.* at 765, 242 N.Y.S.2d at 27. Although the grantor's wife (a New York resident) survived him, the trustee "exercised the granted power to accumulate the trust income, [] filed no [New York] State income tax returns reporting its receipt for the succeeding taxable periods and [] paid no income tax thereon." *Id.* at 765, 242 N.Y.S.2d at 27-28. The State conceded that "the trustee is domiciled in the State of Maryland, that the trust is administered there and that the intangibles constituting its corpus have been at all times in its exclusive possession and control in that State." *Id.* at 765, 242 N.Y.S.2d at 28.

New York's intermediate appellate court sustained the trustee's due process challenge to New York's statutory scheme purporting to authorize taxation of the trust's accrued (undistributed) income. The court acknowledged that the trust "must be deemed a resident trust by statutory definition." *Id.* at 765, 242 N.Y.S.2d at 28 (citation omitted). It reasoned, however, that "the related statutes which impose a tax upon [the trust's] accrued income undertake ... to extend the taxing power of the State to property wholly beyond its jurisdiction and thus conflict with the due process clause of the Fourteenth Amendment." *Id.* at 765-66, 242 N.Y.S.2d at 28 (citations omitted). The court found no merit in the state's "continuing jurisdiction theory." *Id.* at 766, 242 N.Y.S.2d at 28. New York's highest court affirmed, commenting that "[t]he lack of power of New York State to tax in this instance stems not from the possibility of double taxation but from the inability of a State to levy taxes beyond its border." *Mercantile-*

Safe Deposit & Trust Co. v. Murphy, 203 N.E.2d 490, 491 (N.Y. 1964).

2. ***Potter***

The domicile of the grantor was expressly rejected as a sufficient basis for resident tax treatment in *Potter v. Taxation Division Director,* 5 N.J. Tax 399 (1983). In 1972, the settlor, a New Jersey domiciliary, created an irrevocable *inter vivos* trust "by transferring $25 in cash to ... the sole trustee of her trust." *Id.* at 402. The settlor subsequently transferred further assets to the trustee both during her lifetime and through her will, which was probated in New Jersey in 1976. *Id.* Aside from these historical connections, the trust had no connections with New Jersey:

> All income of the trust is derived from sources outside New Jersey. Since the establishment of the trust, the trust assets, consisting of cash, securities, an interest in a Delaware limited partnership and real property in Massachusetts (disposed of in 1976), have been located and managed outside New Jersey. The beneficiaries and the trustee have resided outside New Jersey at all times since the inception of the trust.

Id. at 402-03. After the trustee filed a 1980 New Jersey income tax return showing no tax due, the State of New Jersey assessed the trust on its undistributed income. *Id.* at 401, 403.

The trustee contended "that imposition of the gross income tax on the undistributed income of this trust violates the Due Process Clause," because there were "insufficient contacts with New Jersey to subject the income of this trust to taxation." *Id.* at 403. New Jersey responded that there was sufficient nexus because "the settlor was a New Jersey domiciliary at the time of the creation of the trust and at the time of her death," and because she transferred assets to the trust "during [her] lifetime and after her death in accordance with her will." *Id.*

The court concluded that "New Jersey does not have the authority to tax this *inter vivos* trust for the tax year in question and, therefore, [the challenged taxing statute] may not constitutionally be applied in the subject case." *Id.* at 405. The court reasoned:

> The ability of the State of New Jersey to tax the undistributed income of this *inter vivos* trust depends on the existence of sufficient contacts and benefits to comply with constitutional due process requirements. The domicile of the settlor at the time of the creation of the irrevocable *inter vivos* trust is not in itself a sufficient contact to support taxation by New Jersey.

Id. at 404. The court rejected New Jersey's theory that protections the state had furnished during previous calendar years could establish taxing jurisdiction for 1980, the tax year in issue:

> Receipt of the principal assets of the trust from the New Jersey domiciliary prior to her death in 1976, and the December 1977 receipt of a substantial portion of the "pour-over" assets from the estate of the New Jersey domiciliary

> are acts which occurred prior to the tax year in question.

Id. at 404-05.[84]

3. *Blue*

In *Blue v. Department of Treasury,* 462 N.W.2d 762 (Mich. Ct. App. 1990), the court found no taxing jurisdiction despite a state statute that defined the trust as a "resident trust" based on the domicile of the grantor. In 1961, the grantor, a Michigan resident, created a revocable living trust that became irrevocable a year later, upon the grantor's death. *Id.* at 763. Between 1982 and 1987, the tax years in issue, the trust's sole income beneficiary was a Florida resident, the sole trustee lived in Florida, "[a]ll of the trust's assets and other indicia of ownership [were] located in Florida ... [and] all brokerage accounts and bank accounts [were] held and administered in Florida." *Id.* The trustee sought to recover taxes paid to Michigan on accumulated trust income for the tax years in issue. *Id.*

Michigan law defined a "resident trust" as "one created by a person domiciled in Michigan at the time the trust became irrevocable." *Id.* (statutory citation omitted). The trustee alleged that resident tax treatment based on this definition violated due process "by attempting to tax activities and assets beyond the boundaries and control of the state." *Id.* Michigan responded "that the continuing residency of the trust within Michigan and the benefits and protections of

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[84] The court further noted that assets entering the trust through probate were subject to the state's inheritance tax, and that distributions exiting the trust to in-state beneficiaries were taxable to the beneficiaries themselves. *Potter,* 5 N.J. Tax at 405.

laws of this state extended to the trust established the requisite nexus and jurisdiction to impose a tax." *Id.* at 764. The court concluded that the challenged statute, by "defining the present trust as a resident trust subject to Michigan income tax, violates the due process clause." *Id.* at 765.

The court first noted that "[a]n income tax is justified only when contemporary benefits and protections are provided the subject property or entity during the relevant taxing period." *Id.* at 764 (quoting *In re Swift,* 727 S.W.2d 880, 882 (Mo. 1987)). It ultimately concluded that "there are insufficient connections between the trust and the State of Michigan to justify the imposition of an income tax ... where neither the trustee nor the trust property are within the state." *Id.* The court found "no ongoing protection or benefit to the trust," especially considering that "[a]ll of the income-producing trust property [was] located in Florida," the sole income beneficiary and the sole trustee were domiciled in Florida, and "[m]ost importantly, the trust [was] administered and registered in Florida." *Id.*

The court emphatically rejected the notion that the state had the power to tax the trust simply because a statute defined it as a "resident trust":

> We are unpersuaded by [Michigan's] arguments that the fact that the trust is defined as a resident trust imparts legal protections and jurisdiction. We find that these protections are illusory considering that the trust is registered and administered in Florida. The state cannot create hypothetical legal protections through a classification scheme whose validity is

> constitutionally suspect and attempt to support the constitutionality of the statute by these hypothetical legal protections.

Id.

4. *Linn*

The court in *Linn v. Department of Revenue,* 2 N.E.3d 1203 (Ill. Ct. App. 2013), likewise ruled that due process prohibited Illinois from taxing a trust's income simply by virtue of a statute that defined the trust as a "resident" based on the grantor's domicile at the time the trust became irrevocable. The Autonomy Trust 3 was created in 2002 from the assets of a pre-existing irrevocable trust established in 1961 by an Illinois resident, *id.* at 1204-05, 1210, who the parties agreed was therefore the grantor of Autonomy Trust 3, *id.* at 1208. In 2006, the tax year in issue, none of the trust beneficiaries were Illinois residents, the trustee "resided in Texas, and the [trust] was administered in Texas. The [trust] had no assets in Illinois." *Id.* at 1206. The trust reported no 2006 income from Illinois sources and thus paid no Illinois tax. *Id.* Illinois, however, "reclassified the [trust] as an Illinois resident under [the definitional statute], taxed 100% of the trust's reported income, and assessed a deficiency liability." *Id.*

Illinois law defined "resident" to include "[a]n irrevocable trust, the grantor of which was domiciled in [Illinois] at the time such trust became irrevocable." *Id.* at 1207-08 (statutory citation omitted). The trustee argued that "[w]ithout any connections to Illinois [in 2006], the imposition of Illinois income tax on the [trust] would be unconstitutional under the due process clause." *Id.* at 1208.

After reviewing the same authorities we have just summarized, the court noted that Illinois had cited "no cases finding a grantor's in-state residency is a sufficient connection for due process with an *inter vivos* trust" and, indeed, that "decisions from other states have found the grantor's in-state residence insufficient to establish a minimum connection." *Id.* at 1210. It next observed that "with income taxation, the focus of the due process analysis is on the tax year in question." *Id.* (citation omitted).

The court found that "no connections appear to exist with the trust in this case." *Id.* at 1208. Moreover, the court specifically concluded that "the fact the Autonomy Trust 3's grantor was an Illinois resident is not a sufficient connection to satisfy due process." *Id.* at 1210. The court thus concluded that "insufficient contacts exist between Illinois and the [trust] to satisfy the due process clause, and thus the income tax imposed on the [trust] for the tax year 2006 was unconstitutional." *Id.* at 1211.

5. *Gavin*

The Commissioner finds support for taxation of the Trusts as "residents" m *Chase Manhattan Bank v. Gavin,* 733 A.2d 782 (Conn. 1999). Although *Gavin* upheld the resident tax treatment of an *inter vivos* trust, that result was supported principally by a factor *other than the grantor's domicile. Id.* at 801-02 ("In the present case, the critical link to the undistributed income sought to be taxed is the fact that the non-contingent beneficiary of the inter vivos trust during the tax year in question was a Connecticut domiciliary."). We have already concluded that consideration of such separate nexus factors when applying section 290.01, subdivision 7b(a)(2), would contravene the will of the Legislature.[85] *See supra* § VI.B. In addition, the court's reasoning in *Gavin* actually supports the Trusts' position that—as a discrete historical connection—the domicile of the grantor alone is not sufficient to justify the resident tax treatment of an *inter vivos* trust:

> [The trustee] also argues that implicit in the due process test for taxation are the requirements "that the benefits provided by the State seeking to tax be contemporaneous with the imposition of the tax," and that there be a nexus between the benefits provided by the state and "the earning of the income which is the

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[85] Even if we could consider the domicile of a beneficiary when evaluating state connection under the grantor-domicile rule, we would place no reliance on that factor. For *Gavin* was incorrectly decided insofar as it relies on the domicile of trust *beneficiaries* as a basis for jurisdiction to tax a trust. *See Safe Deposit & Trust Co. of Balt.,* 280 U.S. at 89-93 (concluding that due process prohibited Virginia from taxing the trustee, a Maryland resident, upon the corpus of a trust (intangible assets held by the trustee) even though the trust's beneficiaries were Virginia domiciliaries); *Brooke v. City of Norfolk,* 277 U.S. 27, 28-29 (1928) (concluding that due process prohibited Virginia from taxing the beneficiary on the entire corpus of a trust (as distinguished from distributions to her) where "the property is not within the State, does not belong to the [beneficiary] and is not within her possession or control"). *See also Kimberley Rice Kaestner 1992 Family Trust v. North Carolina Dep't of Revenue,* 789 S.E.2d 645, 649-51 (N.C. Ct. App. 2016) (reviewing authorities and similarly concluding that the residence of a beneficiary does not confer jurisdiction to tax a trust), *writ allowed,* 793 S.E.2d 683 (N.C. 2016).

> subject of the taxation." To the extent that the first of these implicit requirements, namely, contemporaneity, suggests that the benefits be more than historical, we agree. We think that it is implicit in the due process test that the benefits afforded by the state to a domiciliary, or its functional equivalent, justifying the taxation of its income, must generally span the time period during which the income was earned, and not solely antedate that time period without any continuing effect.

Gavin, 733 A.2d at 801.[86]

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[86] *Gavin* also upheld the state's taxation of four *testamentary* trusts. *Gavin,* 733 A.2d at 785, 790-801. The Commissioner likewise relies on two other testamentary trust cases. *See* Appellee's Mem. Supp. Summ. J. 15-18 (citing *Westfall v. Dir. of Revenue,* 812 S.W.2d 513 (Mo. 1991), and *In re Swift,* 727 S.W.2d 880 (Mo. 1987)). The Trusts contend that testamentary trusts are distinguishable, and that "[t]he case for asserting jurisdiction to tax a testamentary trust based on the domicile of the decedent ... is probably a stronger one because of the connection that a testamentary trust has to the state's probate courts." Appellants' Mem. Supp. Summ. J. 26 n.25. Courts have so reasoned, emphasizing the *ongoing* provision of state protections *to the testamentary trust itself.* In *Gavin,* for example, the court considered "whether the contacts between the testamentary trusts and Connecticut are sufficient constitutionally for Connecticut to treat the trusts as if they were domiciliaries." *Gavin,* 733 A.2d at 793. The court held in the affirmative, noting that Connecticut law provided for the creation of the testamentary trusts and determined their validity. *Id.* at 795. In addition, the State's courts assured "the continued existence of the trusts as mechanisms for the disposition of the testators' property according to the terms of the trusts as provided by the respective wills." *Id.* Another court has noted that "[a] testamentary trust, like a corporation, is a creature of the laws of the state where it is created and owes its

6. Application of Authorities And Conclusion

Each of the foregoing cases involves a state's attempt to tax worldwide income by *defining* an *inter vivos* trust as a "resident." The attempt failed in all but one case (*Gavin*), which is distinguishable. In the other cases, courts determined that the applicable residency definition did not require state connection of sufficient substance to justify resident tax treatment under the Due Process Clause of the Fourteenth Amendment.

In *Potter, Blue, Linn,* and *Gavin*—as in the present case—the "resident trust" definition was based on the domicile of the grantor at the time the *inter vivos* trust became irrevocable. All four courts rejected this

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very existence to those laws." *D.C. v. Chase Manhattan Bank,* 689 A.2d 539, 544 (D.C. 1997). The court concluded "that the Due Process Clause does not prevent the District from imposing [an annual net income tax on the testamentary trust], given the continuing supervisory relationship which the District's courts have with respect to administration of such a trust." *Id.* at 540. In precisely these respects, however, the court distinguished *inter vivos* trusts:

> [T]he nexus between the [inter vivos] trust and the District is arguably more attenuated, since the trust was not created by probate of the decedent's will in the District's courts. An irrevocable inter vivos trust does not owe its existence to the laws and courts of the District in the same way that the testamentary trust at issue in the present case does, and thus it does not have the same permanent tie to the District. In some cases the District courts may not even have principal supervisory authority over such an inter vivos trust.

Id. at 547 n.11. Here, of course, we deal with *inter vivos* rather than testamentary trusts.

historical connection *with the grantor* as sufficient to establish taxing jurisdiction over a trust. To satisfy due process, the courts reasoned, state protections must be contemporaneous with the accumulation of the income to be taxed. Because protections extended to the grantor when the *inter vivos* trust became irrevocable were—by hypothesis—extended *at that discrete historical moment,* they could not support taxing jurisdiction for subsequent tax years. Hoping to highlight the inadequacy of a purely historical connection with the grantor to justify perpetual taxing jurisdiction over a trust, one court commented:

> We analogize the present case to a hypothetical statute authorizing that any person born in Michigan to resident parents is deemed a resident and taxable as such, no matter where they reside or earn their income. We believe this would be clearly outside of the state's power to impose taxes.

Blue, 462 N.W.2d at 764-65.

It is unsurprising that courts have universally rejected state efforts to tax trusts as "residents" based solely on the domicile of the grantor at the time an *inter vivos* trust became irrevocable. As the *Blue* Court's analogy indicates, this manner of asserting jurisdiction over a trust suffers from at least two separate problems.

First, it reaches *back through time* to a discrete historical moment, and purports to rely on state protections extended (to the grantor) at that moment. But as the foregoing cases indicate, due process does not permit this resort to protections provided exclusively in previous tax years: the protections provided "must generally span the time period during which the income was earned, and not solely antedate that time period without any continuing effect." *Gavin,* 733 A.2d at 801. In addition, because the domicile of the grantor at the moment an *inter vivos* trust became irrevocable is a matter of historical fact, it is—as to the trust—an immutable characteristic. Consequently, residency under this factor will be *perpetual,* and the due process problem associated with reaching back through time will worsen with each passing year.

Second, the grantor-domicile method of asserting taxing jurisdiction over a trust reaches *across persons.* Rather than relying on connections *with the trust itself,* it relies instead on connections with the trust's grantor. There is no doubt that domicile establishes a substantial connection between the taxing state and the grantor. But a connection with the grantor at the time the trust became irrevocable does not entail any connection with the trust at that same moment. *Potter* perfectly illustrates the point.

In that case, the New Jersey settlor transferred assets "consisting of cash, securities, an interest in a Delaware limited partnership and real property in Massachusetts" to a trustee residing outside of New Jersey. *Potter,* 5 N.J. Tax at 402-03. In rejecting New Jersey's attempt to tax the trust based on the grantor's domicile, the court noted: "Since the establishment of the trust, the trust assets ... have been located and managed outside New Jersey. The beneficiaries and the trustee have resided outside New Jersey at all times since the inception of the trust." *Id.* at 402-03. Thus, even at the time the grantor created the irrevocable *inter vivos* trust in 1972, the State of New Jersey furnished the trust no real protections.

The infirmity of the grantor-domicile rule is further demonstrated by the relative superficiality of the connection upon which it relies. Even if the grantor's domicile were a cognizable connection *between an inter vivos trust and the taxing state,* that connection would not approach in substance the connections courts have ruled sufficient to justify resident tax treatment. Plainly, it does not compare in substance with domicile—with a trust's *own* domicile in a state.

Under Minnesota law, domicile for a natural person "means the bodily presence of an individual person in a place coupled with an intent to make such a place one's home." Minn. R. 8001.0300, subp. 2 (2015). The substantive quality of domicile is illustrated by the Commissioner's enumeration of 26 factors that "will be considered in determining whether or not a person is domiciled in this state." *Id.,* subp. 3; *Dreyling v. Comm'r of Revenue*, 753 N.W.2d 698, 703-04 (Minn. 2008) (listing the numerous connections to Minnesota establishing the taxpayer as a Minnesota domiciliary). Domicile is equally substantive for an entity. Corporate domicile, for example, is "[t]he place considered by law as the center of corporate affairs, where the corporation's functions are discharged; the legal home of a corporation, usu. its state of incorporation or the state in which it maintains its principal place of business." *Corporate domicile, Black's Law Dictionary* 593 (10th ed. 2014).

The domicile of the grantor likewise does not compare in substance with the connections required by Minnesota's nondomiciliary resident statute: 183 days physically present in Minnesota along with the maintenance of an abode here. Minn. Stat. §290.01, subd. 7(b) (2016). The Minnesota Supreme Court recently explained that the State's nondomiciliary resident statute "in particular serves the purpose of requiring individuals who avail themselves of Minnesota's services, benefits, and protections *through substantial contact with the state* for most of the year *to pay taxes on their entire income." Marks,* 875 N.W.2d at 327 (emphasis added). Although this justification for "resident" tax treatment is not based on domicile, it nevertheless relies on "substantial contact with the state" sufficient to warrant taxing the taxpayer's "entire income." *Id.* Domicile of the grantor involves no such present and substantial connections.

In accordance with the foregoing authorities, we conclude that the domicile of the grantor at the time a trust became irrevocable—standing alone—is not a sufficient basis to justify the resident tax treatment of an *inter vivos* trust. We have previously ruled that the sole state connection we may consider when evaluating residency under section 290.01, subdivision 7b(a)(2), is the domicile of the grantor at the time the *inter vivos* trust became irrevocable. *See supra* § VI.C. Consequently, we conclude that section 290.01, subdivision 7b(a)(2), as applied to the Trusts for tax year 2014, violates the due process provisions of the Minnesota and United States constitutions.[87]

Because Minnesota did not have a sufficient basis to tax the Trusts as "residents," and thus to allocate to itself "[i]ncome or gains from intangible personal

[87] Because we resolve this case on due process grounds, we do not reach the Trusts' Commerce Clause claims.

property *not employed in the business of the recipient,"* Minn. Stat. § 290.17, subd. 2(c) (emphasis added), it was without authority to tax each Trust on: (1) gain from the 2014 FFI stock sale; and (2) 2014 income from the its Wells Fargo investment account (administered in California).[88] Put another way, Minnesota did not have subject matter jurisdiction over gain and income from these items of intangible personal property not located within Minnesota.[89] Consequently, the Commissioner erred in denying the Trusts' refund claims. We grant the Trusts' motions for summary judgment and deny the Commissioner's motions.

B.S.D.

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[88] We reject the Commissioner's contention that *International Harvester Co. v. Wis. Department of Taxation,* 322 U.S. 435 (1944) and *Wis. v. J.C. Penney Co.,* 311 U.S. 435 (1940) support Minnesota's attempt to tax the Trusts' worldwide income without regard to source. *See* Appellee's Mem. Supp. Summ. J. 11-15. Indeed, those cases merely affirm a state's power to tax income *from in-state sources. Int'l Harvester,* 322 U.S. at 442 ("We think that Wisconsin may constitutionally tax the Wisconsin earnings distributed as dividends to the stockholders."); *J.C. Penney,* 311 U.S. at 442, 446 (noting that where the "practical operation of this legislation is to impose an additional tax on corporate earnings within Wisconsin," the "incidence of the tax as well as its measure is tied to the earnings which the State of Wisconsin has made possible").

[89] Our ruling is *not* based on lack of personal jurisdiction over the Trusts, a matter about which we express no opinion.

APPENDIX C

STATUTORY PROVISIONS

Minn. Stat. § 290.01 DEFINITIONS. [Impertinent Subdivisions Omitted]

Subd. 7b. **Resident trust.** (a) Resident trust means a trust, except a grantor type trust, which either (1) was created by a will of a decedent who at death was domiciled in this state or (2) is an irrevocable trust, the grantor of which was domiciled in this state at the time the trust became irrevocable. For the purpose of this subdivision, a trust is considered irrevocable to the extent the grantor is not treated as the owner thereof under sections 671 to 678 of the Internal Revenue Code. The term "grantor type trust" means a trust where the income or gains of the trust are taxable to the grantor or others treated as substantial owners under sections 671 to 678 of the Internal Revenue Code. This paragraph applies to trusts, except grantor type trusts, that became irrevocable after December 31, 1995, or are first administered in Minnesota after December 31, 1995.

(b) This paragraph applies to trusts, except grantor type trusts, that are not governed under paragraph (a). A trust, except a grantor type trust, is a resident trust only if two or more of the following conditions are satisfied:

(i) a majority of the discretionary decisions of the trustees relative to the investment of trust assets are made in Minnesota;

(ii) a majority of the discretionary decisions of the trustees relative to the distributions of trust income and principal are made in Minnesota;

(iii) the official books and records of the trust, consisting of the original minutes of trustee meetings and the original trust instruments, are located in Minnesota.

(c) For purposes of paragraph (b), if the trustees delegate decisions and actions to an agent or custodian, the actions and decisions of the agent or custodian must not be taken into account in determining whether the trust is administered in Minnesota, if:

(i) the delegation was permitted under the trust agreement;

(ii) the trustees retain the power to revoke the delegation on reasonable notice; and

(iii) the trustees monitor and evaluate the performance of the agent or custodian on a regular basis as is reasonably determined by the trustees.

Minn. Stat. § 290.03 INCOME TAX; IMPOSITION, CLASSES OF TAXPAYERS.

An annual tax for each taxable year, computed in the manner and at the rates hereinafter provided, is hereby imposed upon the taxable income for such year of the following classes of taxpayers:

(1) Resident and nonresident individuals;

(2) Estates of decedents, dying domiciled within or without this state;

(3) Trusts (except those taxable as corporations) however created by residents or nonresidents or by domestic or foreign corporations

Minn. Stat. § 290.17 GROSS INCOME, ALLOCATION TO STATE. [Impertinent Subdivisions Ommited]

Subdivision 1. **Scope of allocation rules.** (a) The income of resident individuals is not subject to allocation outside this state. The allocation rules apply to nonresident individuals, estates, trusts, nonresident partners of partnerships, nonresident shareholders of corporations treated as "S" corporations under section 290.9725, and all corporations not having such an election in effect. If a partnership or corporation would not otherwise be subject to the allocation rules, but conducts a trade or business that is part of a unitary business involving another legal entity that is subject to the allocation rules, the partnership or corporation is subject to the allocation rules.

(b) Expenses, losses, and other deductions (referred to collectively in this paragraph as "deductions") must be allocated along with the item or class of gross income to which they are definitely related for purposes of assignment under this section or apportionment under section 290.191, 290.20, or 290.36. Deductions definitely related to any item of gross income assigned under subdivision 2, paragraph (e), are assigned to the taxpayer's domicile.

(c) In the case of an individual who is a resident for only part of a taxable year, the individual's income, gains, losses, and deductions from the distributive share of a partnership, S corporation, trust, or estate are not subject to allocation outside this state to the extent of the distributive share multiplied by a ratio, the numerator of which is the number of days the individual was a resident of this state during the tax year of the partnership, S corporation, trust, or estate, and the denominator of which is the number of days in the taxable year of the partnership, S corporation, trust, or estate.

Subd. 1a. [Repealed, 1987 c 268 art 1 s 127]

Subd. 2. **Income not derived from conduct of a trade or business.** The income of a taxpayer subject to the allocation rules that is not derived from the conduct of a trade or business must be assigned in accordance with paragraphs (a) to (f):

(a)(1) Subject to paragraphs (a)(2) and (a)(3), income from wages as defined in section 3401(a) and (f) of the Internal Revenue Code is assigned to this state if, and to the extent that, the work of the employee is performed within it; all other income from such sources is treated as income from sources without this state.

Severance pay shall be considered income from labor or personal or professional services.

(2) In the case of an individual who is a nonresident of Minnesota and who is an athlete or entertainer, income from compensation for labor or personal services performed within this state shall be determined in the following manner:

(i) The amount of income to be assigned to Minnesota for an individual who is a nonresident salaried athletic team employee shall be determined by using a fraction in which the denominator contains the total number of days in which the individual is under a duty to perform for the employer, and the numerator is the total number of those days spent in Minnesota. For purposes of this paragraph, off-season training activities, unless conducted at the team's facilities as part of a team imposed program, are not included in the total number of duty days. Bonuses earned as a result of play during the regular season or for participation in championship, play-off, or all-star games must be allocated under the formula. Signing bonuses are not subject to allocation under the formula if they are not conditional on playing any games for the team, are payable separately from any other compensation, and are nonrefundable; and

(ii) The amount of income to be assigned to Minnesota for an individual who is a nonresident, and who is an athlete or entertainer not listed in clause (i), for that person's athletic or entertainment performance in Minnesota shall be determined by assigning to this state all income from performances or athletic contests in this state.

(3) For purposes of this section, amounts received by a nonresident as "retirement income" as defined in section (b)(1) of the State Income Taxation of Pension Income Act, Public Law 104-95, are not considered income derived from carrying on a trade or business or from wages or other compensation for work an employee performed in Minnesota, and are not taxable under this chapter.

(b) Income or gains from tangible property located in this state that is not employed in the business of the recipient of the income or gains must be assigned to this state.

(c) Income or gains from intangible personal property not employed in the business of the recipient of the income or gains must be assigned to this state if the recipient of the income or gains is a resident of this state or is a resident trust or estate.

Gain on the sale of a partnership interest is allocable to this state in the ratio of the original cost of partnership tangible property in this state to the original cost of partnership tangible property everywhere, determined at the time of the sale. If more than 50 percent of the value of the partnership's assets consists of intangibles, gain or loss from the sale of the partnership interest is allocated to this state in accordance with the sales factor of the partnership for its first full tax period immediately preceding the tax period of the partnership during which the partnership interest was sold.

Gain on the sale of an interest in a single member limited liability company that is disregarded for federal income tax purposes is allocable to this state as if the single member limited liability company did not exist and the assets of the limited liability company are personally owned by the sole member.

Gain on the sale of goodwill or income from a covenant not to compete that is connected with a business operating all or partially in Minnesota is allocated to this state to the extent that the income from the business in the year preceding the year of sale was assignable to Minnesota under subdivision 3.

When an employer pays an employee for a covenant not to compete, the income allocated to this state is in the ratio of the employee's service in Minnesota in the calendar year preceding leaving the employment of the employer over the total services performed by the employee for the employer in that year.

(d) Income from winnings on a bet made by an individual while in Minnesota is assigned to this state. In this paragraph, "bet" has the meaning given in section 609.75, subdivision 2, as limited by section 609.75, subdivision 3, clauses (1), (2), and (3).

(e) All items of gross income not covered in paragraphs (a) to (d) and not part of the taxpayer's income from a trade or business shall be assigned to the taxpayer's domicile.

(f) For the purposes of this section, working as an employee shall not be considered to be conducting a trade or business.

Subd. 3. **Trade or business income; general rule.** All income of a trade or business is subject to apportionment except nonbusiness income. Income derived from carrying on a trade or business must be assigned to this state if the trade or business is conducted wholly within this state, assigned outside this state if conducted wholly without this state and apportioned between this state and other states and countries under this subdivision if conducted partly within and partly without this state. For purposes of determining whether a trade or business is carried on exclusively within or without this state:

(a) A trade or business physically located exclusively within this state is nevertheless carried on partly within and partly without this state if any of the principles set forth in section 290.191 for the allocation of sales or receipts within or without this state when applied to the taxpayer's situation result in the allocation of any sales or receipts without this state.

(b) A trade or business physically located exclusively without this state is nevertheless carried on partly within and partly without this state if any of the principles set forth in section 290.191 for the allocation of sales or receipts within or without this state when applied to the taxpayer's situation result in the allocation of any sales or receipts within this state. The jurisdiction to tax such a business under this chapter must be determined in accordance with sections 290.014 and 290.015.

…

Subd. 6. **Nonbusiness income.** Nonbusiness income is income of the trade or business that cannot be apportioned by this state because of the United States Constitution or the Constitution of the state of Minnesota and includes income that cannot constitutionally be apportioned to this state because it is derived from a capital transaction that solely serves an investment function. Nonbusiness income must be allocated under subdivision 2.